

SUBMISSION
BY THE
ONTARIO FEDERATION OF LABOUR

ESTABLISHING A SINGLE
FINANCIAL SERVICES REGULATOR

June 27, 2001

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On behalf of our 650,000 affiliated trade union members, the Ontario Federation of Labour is pleased to submit a response to the April Consultation Draft, “*Establishing a Single Financial Services Regulator*”.

Attached as Appendix A is our submission of October 3, 2000, to the consultation held by the Parliamentary Assistant, Mr. David Young.

Our trade union members who are members of defined benefit plans are totally dependent on the provincial pension regulator for the protection of their deferred vested benefits.

There is much speculation about a so-called decline of membership in defined benefit plans. But in fact, 49% of members belonging to registered pension plans belong to defined benefit plans. And another 36% of registered plan members belong to Multi-employer defined benefit plans. Only 14% of plan members belong to defined contribution plans.

Since 1996 there has been an increase of 164,000 plan members belonging to defined benefit plans in Ontario.

1. Separate Pension Division

We are pleased to see that one of our principal recommendations, that there be a separate pensions division within the new Financial Services Organization, with a separate Superintendent of Pensions and a separate pensions tribunal, has been accepted.

We believe that this measure is essential to effective regulation and protection of registered pension plans. We have had grave concerns since the beginning of the financial services merger process. The pension sector is radically different from all the other financial services which are being merged under the one roof. Mortgages, loans and trust companies, investment dealers, banks and credit unions and insurance companies are all involved in selling their financial products in a market. It is properly the function of the FSO to ensure the integrity and honesty of this market. For those sectors who retail their products in a market, the merger makes sense.

But pensions are not a retail product. Employees do not buy our pension plans in a market. We negotiate them, in hard bargaining, as adversaries, at the bargaining table. The results of our negotiations are imbedded in our collective agreements. Our pensions are not a commodity which we have purchased. They are our deferred wages which are held in a fiduciary trust for our future use. Our trade union officers and staff are obliged to monitor, and, where possible participate in the administration of our pension plans to ensure that our members’ interests are protected. That obligation is even enshrined in law and is a consequence of the “duty to represent” provision of the *Ontario Labour Relations Act*.

Mixing the regulation of pensions with the regulation of the rest of the financial services sector is an incompatible mixture. At the very least, a separate pension division is a fundamental necessity.

2. The Pension Tribunal

We strongly support the continued existence of a separate Pension Tribunal. However, if this tribunal is to function fairly and effectively it must be representative of both workplace parties. Its predecessor, the Pension Commission of Ontario, provided a valuable forum where pension disputes could be resolved, often short-circuiting the need for a hearing at all. This trend has continued under the present FSCO tribunal. But we believe that, for this important dispute-settlement function to continue under the new tribunal, its membership must be a balance of skilled and experienced pension stakeholders, including a fair balance of trade union representatives. It will be crucial for the credibility of this new tribunal that experienced labour representatives continue to participate, and in more than a token manner. This credibility will be essential if pension disputes are to be kept out of the Courts.

We also support the provision in S39(3) of the draft bill that “*a panel may consist of one or more members*”. In other words, there is no necessity at all for a member of the Commission to sit on every panel. Indeed, such a requirement would entirely negate and frustrate the purpose of the Pension Tribunal.

3. The Commission; Governance

The proposed governance structure for the new Financial Services Organization may be appropriate for the broader financial services sector. But it is completely inappropriate for the pension sector.

We understand it is contemplated that only 3 of the 18 Directors of the Commission would be drawn from the pension sector. Presumably, virtually all of the Directors will be drawn from the business community.

Yet it is proposed that far-ranging powers to make policy, including pension policy, will be vested in this very one-sided Commission. It will also have significant rule-making powers, which will replace and have the legal force of Regulations under the Act.

It is impossible for us to accept a Governance structure which is given such enormous powers over key provisions of our contracts with our employers as well as our property interest in our deferred vested benefits - from which we are entirely excluded!

Our position remains that the proper Governance structure for a Commission regulating the pension sector would include balanced representation from pension stakeholders, including equal representatives of labour and management, along with members of the pension bar and other independent pension experts.

Government may well find the notion of equal representation for labour on the new Financial Services Commission as preposterous.

But just how preposterous is it to empower a small Commission drawn exclusively from the business community with far-reaching policy and rule-making powers over our contracts and vested benefits ...and to exclude us totally from the Governance process?

It speaks again to the folly of squeezing pension regulation into a merger where it does not belong. But it still creates major problems of fairness, balance and credibility which cannot easily be overcome.

We would strongly advise the appointment of significant labour representation to the new Commission. Failing that, we would expect to see significant representation on the Commission from the labour pension bar.

We do expect that labour will be adequately represented on the Advisory Committee proposed in S91 of the Draft. And we have a proposal for a Pensions Advisory Committee which we feel is essential given our concerns about the total lack of balance on the proposed Commission.

4. A Pension Advisory Committee

We recommend the establishment of a Pension Advisory Committee which would support the work of the FSO pension division in a number of ways.

- It would be composed of an equal balance of labour and management representatives with pension experience, together with representatives of the labour bar and independent pension experts.
- It would review proposed pension rules as they are being formulated by the Commission, prior to the period of public consultation.
- It would provide a forum to discuss, review and even originate policy proposals. At the present time, the Draft contains no clear outline of a process to be followed for policy development. Given the lack of representation from the pension sector on the Commission, and the lack of balance, this is a major problem. The Draft bill, at S90, requires the Tribunal to consider any relevant policy made by the Commission. Yet the Commission as a body will lack pension expertise and knowledge and will be totally one-sided in its makeup.

We believe that pension stakeholders must be involved at the front end in the development of pension policy. A separate Pension Advisory Committee would be a useful forum for the review of pension policy proposals at the initial stage of policy development.

We recommend that the Draft legislation be amended to provide the statutory authority to establish a Pension Advisory Committee.

5. Rules

With respect to the new rule-making powers of the Commission, we have already set out our concerns about labour's complete exclusion from the proposed Board of Directors which will exercise the rule-making power.

We stress again how extraordinary these new powers are. A small Commission which we fear will be drawn only from one sector of the community - the business sector - is being given powers to make Regulations under the *Pension Benefits Act* which were hitherto the sole prerogative of the Lt. Governor-in-Council.

We do not condone this bizarre exercise in one-sided empowerment.

And we strongly support the advice that has come from many participants in the consultation: that the new rule-making power must be severely circumscribed and constrained.

In fact, we must insist that the proposed limits on the rule-making power, as set out in the Draft, be maintained in the new legislation.

On page xiii of the Draft it states, "... *There would be no rule-making for areas of substantive public policy*". We have been assured that there would be no rule-making powers in any area which would affect members' individual benefit entitlement.

We have had the opportunity to review the areas proposed for rule-making and the areas to be excluded. We are satisfied that the areas proposed for rule-making by FSCO at this time do properly exclude areas which affect members' benefits. We will continue to be vigilant to ensure that this does not change.

This is a matter of accountability which goes to the heart of our system of democratic government. On matters of substance, the elected government must retain responsibility and accountability. This is especially true in the case of pension regulation, where policy and rules can adversely affect both the contract rights and the property rights of working people.

6. Conflict of Interest

Finally, we note the sad fact that the Draft Bill is silent once again on the subject of conflict of interest which continues to bedevil the pension sector.

As we have documented time and again, the pension industry tolerates conflict of interest as a matter of routine. Attached in Appendix C is a copy of a letter from Mr. Hugh Mackenzie, research director

of the United Steelworkers union and a member of the OFL Pension Committee, to the Financial Services Commission setting out our position in greater detail.

It is common practice, indeed the norm, for pension actuaries to serve as actuaries to a registered pension plan, and at one-and-the-same time, work as paid actuarial “consultants” to the employer who is the sole trustee of the same pension plan. Routinely, during collective bargaining, we find ourselves sitting across the bargaining table from the actuary of our own pension plan who is acting as the agent of the employer and bargaining against us.

In the legal profession, such outrageous conflict behaviour would be grounds for being disbarred. In Ontario’s pension sector, it is routine.

There are numerous adverse consequences to pension plan members arising from this intolerable state of affairs.

- It is virtually impossible to rely on actuaries acting in this two-sided capacity for accurate information about the true cost of pensions or pension improvements. We are required to retain independent actuaries to obtain accurate information about our own pension plans. What an outrageous situation, when we are obviously unable to trust the actuary of our own pension plan!
- Actuaries are violating the adverse amendment provisions of the *Pension Benefits Act* by misrepresenting the true impacts of plan amendments. This includes the case of an amendment to the FSCO converting a defined benefit plan to a defined contribution plan.
- The actuarial profession steadfastly refuses to acknowledge or accept the basic ethical proposition that the pension actuary stands in a fiduciary capacity to the members of the pension plan as a matter of professional obligation. In the case of *Tremblay v. Falconbridge Ltd. et al, 1999*, summary attached as Appendix B, the pension actuary cited as his defence that as the actuary for the pension plan, he did not have any fiduciary obligation to the members of the pension plan. This was his defence in a court of law, in the province of Ontario, in the year 1999!

It is time, long overdue, for the Government to end this utterly disgraceful state of affairs.

We propose that the new legislation amend the *Pensions Benefit Act* with a provision that requires all administrators, trustees, and their agents, *including members of the actuarial profession*, to act in a fiduciary capacity to the members of a pension plan.

Conclusion

Over the past four years, we have developed a very positive working relationship with the officials at FSCO and the Superintendent of Pensions. The OFL Pension Committee has served as an advisory committee to FSCO and our Director of Legislation sits on the FSCO Advisory Council. We are prepared to continue this positive working relationship with the new Financial Services Organization toward the goal of protecting the rights, interests and deferred vested benefits of the members of pension plans. Our views, set out in this brief and in other forums, are based solely on this goal of protecting the interests of our members and as they arise from the day to day experience of our trade union staff who administer the pension provisions of our collective agreements. We hope they will receive a favourable consideration.

Respectfully submitted.

Ontario Federation of Labour

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APPENDIX “A”

SUBMISSION TO DAVID YOUNG, MPP FINANCIAL SERVICES REGULATION

The Ontario Federation of Labour represents 650,000 affiliated trade union members across Ontario.

The Ontario labour movement's interest in pension matters is long-standing, and all of our affiliated unions are directly involved in pension plan administration. Pension plans and pension benefits exist in our collective agreements entirely as a result of collective bargaining. It is incumbent upon us to monitor all aspects of pension plan administration in order to protect the economic interests of our members and to fulfill our statutory duties under the *Labour Relations Act*.

In the performance of these responsibilities, we have always tried to work closely with the Pension Regulator for the Province of Ontario. Since our relationship with the Regulator extends back in time, it might be profitable to review some of the history of pension regulation in this province.

Prior to the passage of the current *Pension Benefits Act* in 1987, pension regulation in Ontario suffered from a kind of systemic neglect. Pension plans were allowed to run actuarial insolvencies under the nose of the Superintendent. The result: spectacular scandals during the early 1980s when workers at companies like CCM lost their jobs through plant closures only to discover that their pension plans were bankrupt and they were penniless.

Other companies, eg. Conrad Black's Dominion Stores, took advantage of a regulator who was asleep at the switch to expropriate pension funds which legally were the property of his employees. Mr. Black was stopped, and restitution of \$50 million was made to the workers. But it was the Courts who stopped him - not the Superintendent of Pensions for Ontario who had approved the deal.

As a result of a series of similar scandals, the *Act* was overhauled by the Provincial Government between 1985 and 1987. But much of the groundwork was set out in the work of Ontario's Select Committee on Pensions which sat in the early 1980s during the Davis era.

The reformed *Pension Benefits Act* of 1987 remains an important model for the labour movement for a number of reasons.

1. It required a pro-active stance by the Regulator to enforce the fiduciary trust over pension plan funds on behalf of the owners of the funds – Ontario employees. But it also covers a wide range of other issues that are important to plan members and their families.
2. It provided a forum where the two workplace parties, management and labour, could meet and systematically resolve pension disputes outside of the Courts.
3. It provided a policy forum wherein management, labour and government met regularly to review and improve pension policy and pension administration through the PCO.

We understand that the present government has a different policy with respect to pension administration, but we will continue to advocate for a separate Pension Commission, staffed by experts in pension administration, issues and jurisprudence, and composed of representatives of the workplace parties working in co-operation with government.

With this very brief introduction, we can respond to the questions set out in the Discussion Paper.

Question 1

The vision and scope of the proposed Regulator, as set out on pp. 7 & 8, are seriously flawed, inasmuch as pension matters do not belong logically or administratively with the financial services sectors merging into the new OFSC.

The administration of pension plans is NOT simply a matter of managing capital investment. There are a host of issues involved in the administration of the *Pension Benefits Act* which have nothing to do with investment regulation. And there are a host of issues that arise from the fact that pension plans and pension benefits are the subject of collective bargaining under the *Labour Relations Act*. Every collective bargaining table deals with pension issues as part of the overall wage package. All aspects of pension administration are caught up in the relationship between employers and employees at the bargaining table.

This includes the actuarial assumptions used by employers to calculate the dollar cost of pension improvements, the use or disposal of actuarially surplus funds, the provision of spousal and survivor benefits, the governance of pension plans – and much more besides.

None of this has anything to do with the consumer protection function of the Ontario Securities Commission – or the protection of consumers in the insurance, mutual fund, mortgage or loan and trust markets.

The confusion lies in assuming that the pension sector is a financial market like the “other” financial services.

The pension sector is not a market, with willing buyers and sellers and the concomitant need for basic consumer protection. The pension sector is largely an aspect of labour relations. Pension plans are not commodities traded in a free market. They result from the collective bargaining relationship between employees and employers – with all the dynamic complexity and unique jurisprudence of those relationships. We do not ‘buy’ a pension plan, the way a customer buys a stock or a mortgage. We bargain for it, in hard bargaining that is more often than not a bitter contest.

Questions 2, 3, & 4

Having made the above point, it is clear that the government is proceeding with yet another amalgamation of pension regulation, regardless of the basic fact that pension regulation does not fit in with or belong to those financial services which are traded as commodities in markets.

It is not sufficient that there be a separate Pension Tribunal to hear appeals against decisions of the Superintendent of Pensions.

- 1) There must be a separate pensions division within the Financial Services Organization, whatever it is called. Its mandate must be the regulation of the pension industry to protect the whole range of pension plan members’ interests.

This separate pensions division must be staffed with pension experts who understand the nature of pension regulation in all its aspects. This division must have the capacity to monitor plans, enforce the *Act* and provide up-to-date information to the army of union representatives who administer the pension provisions of collective agreements. If expert staff resources are insufficient, Ontario will have more major scandals involving the pension sector.

- 2) There must continue to be a separate Superintendent of Pensions who will continue to be responsible and accountable through the Minister for the administration of the *Pension Benefits Act* and the regulation of the pension industry.

We have made numerous submissions to the existing FSCO on the fact that the pension sector is rife with systemic conflict of interest. We will be pleased to continue these discussions with the successor Regulator. But we are not prepared to see our members’ interests sacrificed to a bogus model of self-regulation when we are systematically excluded from effective partnership in pension matters. We continue to insist that it is government which has the responsibility for ensuring honest and effective pension administration according to the law – and no one else.

Questions 5 & 6

On the issue of the Pension Tribunal, we feel that it is absolutely essential that a separate Pension Tribunal be established. There is a large specialized body of pension law and jurisprudence, and the administration of the *Pension Benefits Act* is a specialized field requiring experience and expertise. Whatever expertise exists within the OSC respecting the *Securities Act* is quite simply irrelevant to the pension sector.

With respect to the structure of a Pension Tribunal, it would be possible to create the space for a separate Pension Tribunal within the proposed new Financial Services Commission, but it will take a special effort and dedicated resources and staff.

The new Commission could indeed consist of a number of members who would chair special purpose pension panels, subject to two conditions. Firstly, these “pension” Commissioners **must** be experts in pension matters and they must be genuinely neutral. The labour movement will not tolerate a stacked Pension Tribunal dominated by decision-makers with an obvious management bias. Secondly, there must be a pool of members to select for a Pension Tribunal who are representative of labour. We remain deeply concerned that the last vestiges of labour representation will be lost in this latest shuffle.

It has been the policy and practice in Ontario for over 15 years that the administrative tribunal dealing with the adjudication of pension disputes had labour representatives on the panel. At the present time, there are only two labour representatives on the FSCO Pension Tribunal. It would be extremely helpful to increase this number, and there is no shortage of pension expertise within the trade union community.

Questions 7, 8, 9, 10 & 11

On the issue of rules, the obvious questions for us is – who will make the rules?

If the proposal is that a Commission which will be composed entirely of non-labour members should be empowered to write rules governing the items set out on p. 16, the answer is, absolutely not. To empower a Commission of business and management representatives with rule-making power over “employer funding obligations,” surplus pension payments, benefit guarantees, and wind-up would be an outrageous conflict of interest. We repeat again that pension plans are not traded as commodities between buyers and sellers. They are the subject of tough collective bargaining between employers and the bargaining agents for employees. And pension funds are deferred wages held in a fiduciary trust in pension plans. To turn the law-making authority for pension administration and regulation to a one-sided consortium of management commissioners would make an utter mockery of pension regulation.

Of course, rule-making in the pension sector could be a viable model if, and only if, there was a proper balance between management and labour representatives on the rule making body.

Since that proposal is not on the table, we insistently demand that for the pension sector, substantive regulation-making authority must continue to be rested in the Lt. Governor in Council.

Question 12

The existing *Pension Benefits Act* contains ample provisions for the effective regulation of the pension sector. We have made a number of constructive suggestions to the FSCO, for example, on the more effective use of Internet communications, which we would be pleased to discuss further.

Questions 13 & 14

It must be stressed that the responsibility for ensuring the honest and effective administration of the *Pension Benefits Act* rests with the Minister. If there is a recurrence of the examples of legalized theft of workers' wages that characterized pension regulation in Ontario prior to 1987, it will be the Minister who is held accountable. There can be no arms-length escape from the obligation to protect workers' deferred wages from irresponsible employers who have demonstrated time after time after time that they are only too willing to break the law.

As you can see, we do not embrace this new initiative with open arms, and that is because our day-to-day experience of pension administration by the employer trustees of our pension plans is extremely negative. There is no partnership in pension administration, the relationship is almost entirely adversarial and we confront regular and systemic attempts by employers to circumvent or flatly violate the law.

We have enjoyed an excellent working relationship with the FSCO and are prepared to work constructively with its successor for the better protection of our members in registered pension plans.

We hope that our suggestions outlined above are given serious consideration. There is a real danger that the existing pension regulator will be completely swallowed-up in a new organization which provides a function that has little or nothing to do with pension regulation and the protection of pension plan members. That would be a great tragedy for our members, and it would have severe consequences for any government which allowed it to happen.

The OFL Pension Committee will be pleased to continue, as we have over the past six years, to consult with the Commission on matters of mutual interest.

Respectfully submitted,

Ontario Federation of Labour

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APPENDIX “B”

PENSION PLAN BENEFICIARIES CAN SUE PLAN ACTUARIES FOR BREACH OF FIDUCIARY DUTY

In the context of a motion for certification of an action as a class proceeding, the Ontario Superior Court of Justice has recently ruled that a group of former pension plan members may proceed in its action against the former actuaries of the plan for breach of fiduciary duty. The actuaries asserted that, in the absence of a fiduciary obligation existing toward a pension plan's beneficiaries, there could be no "common issue" for purposes of a class proceeding.

The Plaintiffs are employees or former employees of Kidd Creek Mines Ltd. (now a division of Falconbridge Limited) (the "Company"), and were formerly members of the company's defined benefit pension plan (the "Plan"). In January 1986, the Company terminated the Plan, and replaced it with a mandatory defined contribution Group RSP arrangement to continue to provide retirement benefits for its employees. When the Plan was terminated, accrued past-service credits attributable to each member were either transferred to the Group RSP (the "Conversation Option"), or alternatively, were used to purchase a deferred pension annuity from an insurance company for the future benefit of the member (the "Deferred Annuity Option"). The amount transferred on behalf of each member was calculated in accordance with, and based upon, actuarial advice provided to the Company by the Alexander Consulting Group (now Sedgwick Limited) (the "Actuary").

Although employees had to elect which option they preferred, the employees allege that the Company "strongly encouraged" them to elect the Conversation Option, and promised them a "special bonus" and "improved entitlement" that was not available under the Deferred Annuity Option. They claim the Company and Actuary used aggressive and inappropriate actuarial and economic assumptions in calculating the Plan's liabilities, and that they were never advised of these assumptions.

Although the Pension Commission of Ontario (as it was then known) ("PCO") originally questioned some of the actuarial assumptions, it ultimately approved the transfer of Plan assets to the Group RSP as well as the partial wind-up report prepared by the actuary. The Company later applied for and obtained the consent of the PCO for the withdrawal of over \$11 million in surplus funds from the Plan, in the absence of providing notice to the employees.

The employees ultimately initiated a class proceeding against the Company, the Actuary and the PCO when it became apparent that the Company had withdrawn the surplus out of the Plan without notice, and when account balances in the new Group RSP were lower than expected. The employees claim negligence, negligent misrepresentation and breach of trust against the Company and Actuary in respect of the allegations, and breach of natural justice and procedural fairness against the PCO for failing to providing due notice to them of the company's surplus application.

With one exception, all of these claims were consented to by the defendants at the class proceedings motion as valid causes of action and issues common to all employees in the plaintiff class. The exception was in relation to the issue of whether an actuary can stand in a fiduciary relationship with a pension plan beneficiary where there is no contractual relationship or other proximity between them. The actuary argued that no such relationship existed with the plan's members and that, in the absence of a valid cause of action against it, this aspect of the claim should not be certified as a common issue.

In support of its claim against the actuary, the employees alleged that although the actuary was retained by the company to perform actuarial services, the fiduciary relationship in respect of the plan members arose "from the nature of the duties that [the actuary] was retained to perform, the discretion accorded to an actuary in respect of future assumptions and the fact that monies being dealt with were trust funds". The employees relied on cases such as *Froese v. Montreal Trust Co. of Canada* (1996), 11 C.C.P.B. 233 (B.C.C.A.), for support for the proposition that pension plan beneficiaries are particularly vulnerable, and in a position of trust with those who act to assist in the administration of the plan, including actuaries.

The Court determined that this was a novel claim since no Canadian court has determined in a *dispositive* manner whether a pension plan actuary can stand in such a fiduciary relationship to a pension plan beneficiary. In applying the principle that "novelty is not a bar to an action," and recognizing that fiduciary relationships did not depend on the identity of the individuals or entities involved, but rather on the nature of the relationship, the Court determined that it was not "plain and obvious" that the employees' cause of action would not succeed.

The Court also rejected the Actuary's alternative argument that the pleadings did not set out a sufficient factual basis for the claim. In its view, the statement of claim disclosed sufficient material

facts to support an allegation that there was a breach of fiduciary duty. The motion for certification was accordingly granted.

In the interests of judicial economy, the Court also addressed the issue of hearing the judicial review application concerning the PCO's conduct and decisions regarding the Plan's surplus, which would normally be heard by the Divisional Court. In holding that the judicial review issues were an essential aspect of the class proceeding, the Court decided that it would also hear and decide the application for judicial review.

The Actuary has sought leave to appeal the decision to the Divisional Court, which application for leave will be heard this autumn.

Ref.: Tremblay v. Falconbridge Ltd. et al., [1999] O.J. No. 2403 (Ont. S.C.J.), reasons for decision June 25, 1999, per Winkler Jr.

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APPENDIX “C”

August 27, 1999

Ms. Dina Palozzi
Superintendent
Financial Services
Commission of Ontario
5160 Yonge Street, 4th floor
Toronto, Ontario
M2N 6L6

Re: Actuary conflict of interest

Dear Ms. Palozzi:

As you will recall, I was part of an OFL contract group which met with you and officials from the Financial Services Commission of Ontario in February of this year.

At that meeting, the OFL group initiated an extended discussion of the implications for pension plan members and beneficiaries of the trend towards self-regulation in the new administrative procedures of the Commission.

One of the issues we raised concerned the importance of detailed, appropriate and timely notification of plan members and/or their representatives of any and all proceedings involving their pension plans. We noted that the current requirement of plan sponsors that documents be provided to plan members or their representatives on request is inadequate in the new context of expedited procedures that enhance the role of the Superintendent relative to that of the Tribunal. We made a number of suggestions, including that of providing a World Wide Web based service listing and providing the current status of all current proceedings.

Ross McClellan will be contacting you separately to follow up respect to these issues.

This letter deals with the issue of the adequacy of the professional standards of actuaries both in the abstract and more particularly in the context of the increased reliance on actuarial opinion and certification in the new, streamlined administrative structure. You had asked that we raise the issue in a more formal

submission that could serve as the starting point for a more extensive review of the question.

It is our view is that an actuary or actuarial firm which acts at the same time as actuary to a pension plan and as an advisor on pension and other matters to the employer/plan sponsor is in a conflict of interest.

As the actuary to a pension plan, the actuary has a fiduciary obligation to the members and beneficiaries of the pension plan. That obligation includes the obligation to protect the interests of the plan members, to ensure that plan members are aware of issues that affect their interests, and to ensure that other interested parties including the plan sponsor, plan trustees and regulatory authorities are made aware of those interests.

As the actuarial advisor to the employer/plan sponsor, the actuary has a duty to his or her client to advance the client's interests.

In general, those interests cannot be expected to coincide. Even in the day-to-day operation of a pension plan, the choice of actuarial assumptions will affect the cash flow of the plan sponsor on one hand, and the security of benefits of plan members and beneficiaries on the other. The more conservative the assumptions, the more secure the benefits, and vice versa.

There are very few choices made in pension plan actuarial work that could not, under some circumstances, adversely affect the interests of plan members and beneficiaries. Were that not the case, actuarial science would amount to nothing more than complicated arithmetic and an actuary could be replaced by any one of a number of good computer programs available on the market.

It is in the area of collective bargaining, however, in which the conflict of interest is most apparent. Here the interests of plan members are represented by a trade union in collective bargaining. The interests of the employer are put forward by the employer's employees and agents. That the economic interests of the parties are in conflict is not debatable.

Yet it is common, if not routine, for the same actuarial firm - and in most cases, the same individual actuary - to be involved in collective bargaining as an actuarial advisor to the employer/plan sponsor.

Our contention is that it is "per se" a conflict of interest for an actuary to serve as the actuarial advisor to a plan sponsor in collective bargaining -- or in a non-union setting in compensation policy determination - and the actuary to the pension plan of which the employer is the sponsor.

Such a conflict is not easily resolved. In our view, it could only be resolved by obtaining the informed consent, of all pension plan members and beneficiaries, to the dual role of the actuary. This is a practical impossibility.

It certainly cannot be resolved through the device currently in vogue among actuaries of characterizing one role as that of an actuary and the other as that of a "consultant". This reduces professional obligation to that of keeping track of various "hats" worn by the actuary at various times and defined by him or her for his or her convenience.

The approach to such conflicts on the part of the actuarial profession stands in sharp contrast to that taken by the most closely analogous professions, the accounting and legal professions. It is inconceivable that an accountant or lawyer would put accept conflicts as transparent as those accepted by actuaries as a matter of routine.

Once it is recognized that the administration of pension plans involves fiduciary responsibilities to plan members and beneficiaries, the practice of serving both the plan and the plan sponsor becomes untenable.

While this is obviously a matter of general concern to legislators and the courts, it ought to be a matter of specific concern to pension regulators.

The Financial Services Commission of Ontario and its predecessor the Pension Commission of Ontario have always relied on the opinions of actuaries in the exercise of their regulatory responsibilities. They have relied on the accuracy of the actuary's calculations in determining the funded status of pension plans and on the certificate of the actuary indicating contribution requirements. They have relied on the assertion of the actuary that amendments submitted for registration are both legitimate given the origins of the plan and accurately reflective of what plan members and beneficiaries expect their benefits to be.

It is implicit in our stated position here that we believe that even the historic reliance of regulators on statements by actuaries is not merited, given endemic conflicts of interests.

Recent regulatory developments, however, heighten our concern. Reliance on filings by actuaries on behalf of plan sponsors has traditionally been buttressed by safeguards. The requirement for regulatory "approval" of changes in the status of pension plans implied, at least in theory, that officials of the Commission actively reviewed the submissions made by actuaries and the assumptions on which they were based. In addition, the role of the Commission as the appeal body for all administrative decisions provided a safeguard accessible to plan members and beneficiaries and their representatives.

In the new regulatory system in Ontario, the Financial Services Tribunal is no longer serves as an appeal level for all decisions of the Superintendent of Financial Institutions as was the case with the former Pension Commission of Ontario. The Superintendent now has final decision making authority in a wide range of matters.

Furthermore, it is intention of the regulator to rely extensively on the attestations of actuaries with respect to such critical questions as whether or not an amendment is an "adverse amendment", to name just one of a number of areas.

In the new world of self-regulation, the system depends totally on the independence and objectivity of the actuary and on his or her appropriate consideration of the interests of plan members.

The current practices of the actuarial profession provide no assurance of that independence and objectivity. Indeed, they virtually guarantee that conflicts material to the interests of plan members and beneficiaries will arise.

While conflicts of the nature described in this note are commonplace, pension plan members and their representatives rarely have the opportunity to explore such conflicts in any detail. The relationship between an actuary and a pension plan sponsor is private. Even the relationship between an actuary and the administrators and trustees of a pension plan is protected. Under Ontario law, the right of pension plan members to information is limited to official filings and communications between the pension plan and pension regulatory authorities. Other aspects of the

relationship - communications between administrators and/or trustees and agents - are private.

The exceptions arise when these relationships come to the surface in the course of legal proceedings involving pension plan administration. For example, the Steelworkers are in the early stages of legal proceedings on pension administration issues with Stelco and Alcan during which information will inevitably surface concerning the many roles played by these companies' actuaries.

A lawsuit involving the Steelworkers and Cominco, the trial portion of which was concluded last fall, exposed detailed information concerning the role of the company's actuary over a period of over 20 years. The evidence in discovery and at trial showed that the plan's BC-based actuary had served as an advocate in support of Cominco's objectives to the exclusion of any consideration of the interests of plan members in every instance, including instances in which the interests of plan members and those of Cominco were clearly different.

This evidence was so compelling that the union will be filing a detailed complaint with the Institute of Actuaries. (The union will also be filing a complaint against the Toronto-based actuary who served Cominco as an expert witness.)

We also asked our legal counsel in the Cominco matter to prepare a memorandum concerning the adequacy of the rules of the Institute of Actuaries with respect to Conflict of Interest and Objectivity.

The union would be prepared to share this information with the Commission at the appropriate time.

Since the purpose of pension regulation is to ensure that the interests of plan members are protected, unresolved and endemic conflicts of interest among actuaries undermines the integrity of the entire system.

While it would be desirable if the Canadian Institute of Actuaries were to introduce meaningful and realistic conflict of interest rules, we believe that Ontario can and should act directly to ensure that pension plan members and beneficiaries in this province are adequately protected.

First, the fiduciary obligations of actuaries and other agents and administrators of pension plans should be spelled out, either in the Act or in regulations.

Second, it should be considered "per-se" a conflict of interest for the same, or a related actuarial firm to act simultaneously as the actuaries to a pension plan and as advisors or consultants on pension matters to an employer who is, directly or indirectly, a sponsor of that pension plan.

We look forward to discussing this with you further.

Yours truly,

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