SUBMISSION

BY THE

ONTARIO FEDERATION OF LABOUR

SURPLUS DISTRIBUTION

FROM

DEFINED BENEFIT PENSION PLANS

SEPTEMBER 6, 2001

On behalf of our 650,000 members, the Ontario Federation of Labour is pleased to respond to the consultation paper, *"Surplus Distribution From Defined Benefit Pension Plans"*.

Our most recent figures, provided by the Financial Services Commission, indicate that over 900,000 workers in Ontario belong to single employer defined benefit pension plans. A second group of 666,000 workers belong to multi-employer defined benefit plans. Altogether, 85% of Ontarians who are members of registered pension plans belong to defined benefit plans, while some 14% are members of defined contribution plans.

Despite the often repeated claim that defined benefit plans are dwindling away, the fact is that defined benefit plans are the pensions of choice for our affiliated members. Since 1996 there has been an increase of 164,000 pension plan members who belong to defined benefit plans.

The July Consultation Paper rightly points out that the issue of Pension Surplus Distribution is complicated and complex. We agree. And for this reason the treatment of pension surplus and so-called pension surplus reform demands to be handled with a great deal of caution. We regret that the substance and timing of this paper raises doubt as to whether the Government is serious about consultation. The paper provides a very thin discussion of complex issues, and the brief period allowing for responses, mostly over the summer, makes a useful debate somewhat unlikely.

In this brief we intend to deal with the surplus distribution issues that have the highest priority for the Labour movement.

Joint trusteeship

It is worth pointing out at the outset that surplus distribution is an issue for the 900,000 members of defined benefit plans which are not multi-employer plans, but it is not an issue for the 660,000 members of multi-employer plans who have defined benefit plans. That is because of the Governance structure: multi-employer plans are governed by boards of trustees that are, as a minimum requirement, equally balanced between Employers and Employees.

Section 8(1)e of the Pension Benefits Act requires each multi-employer plan to be governed by a board of trustees "of whom at least half are representatives of members of the multi-employer plan." In multi-employer plans, where there is an equal

partnership, the use and distribution of surplus is decided rationally and sensibly through negotiation and compromise by the workplace parties. It is our view that the ultimate solution to the management of surplus distribution issue lies in real pension reform which will establish a truly balanced relationship between employers and plan members based on equal representation on pension boards.

Danger: proceed with caution

It is not many years since a series of scandals involving the looting of pension plan "surplus" funds by unscrupulous employers forced the Ontario Government to introduce the present Pension Benefits Act (1987). The most notorious of these was the case of the Dominion Stores Pension Plan, where the Company expropriated $50 million of money which belonged to the members of the Pension Plan with the complicity and approval of the Pension Regulator of the day. Fortunately, this attempt at asset stripping was stopped by the Courts. The Court ruled that the Ontario Pension Commission had failed in its fiduciary duty, and a negotiated distribution of the surplus followed. Workers in Ontario have come to rely on the Courts for protection against the expropriation of their property rights which are vested in pension funds.

There are numerous other cases from the recent past which mandate the most extreme caution by Government as it deals with the issue of surplus distribution. The workers at Canada's famous CCM plant were thrown out on the street with a bankrupt pension plan when it shut down in the eighties and it was discovered that the plan was insolvent. Another notorious example was the case of White Farms, where it was the Court which stopped the employer from taking surplus illegally from the pension plan, despite the approval of the Pension Superintendent of the day.

And at the present time, the fate of an entire community, Sault Ste Marie, hinges on the future of Algoma Steel whose future in turn is threatened by a colossal solvency deficiency of some $600 million in the Algoma pension plan. This is entirely the result of decades of totally irresponsible and systematic under funding, first by the CPR and then by its subsequent owners, Dofasco. Both the CCM and Algoma case represent the calamity which can befall workers and entire communities when employers are allowed to escape their pension contribution obligations, and should stand as a constant reminder to law makers of the high stakes involved in pension "reform".

The goals of the exercise

We can completely agree with the goals set out on page 4 of the paper: to balance employer and employee interests, to safeguard pension security, to keep pension issues out of the Courts, to create certainty, resolve inconsistencies and strengthen the Defined Benefit regime and foster negotiated solutions to pension disputes.

Problem is, many of the suggestions in the consultation paper will have exactly the opposite effect, as we hope to demonstrate in this brief.

We are also concerned that there is significant incoherence and even confusion in the paper, which needs to be dealt with before any new legislation is prepared.

At the heart of the confusion is an apparent determination to emphasize the principle of legal ownership when it comes to the rights of Employers, but to ignore the same ownership rights or indeed override them when it comes to pension plan members. The paper is full of references to what Employers can do if they are "clearly entitled on the basis of plan documents." But the paper is totally silent on the property rights which the Court has assigned to pension plan members, and, in fact, in a number of instances, which we will discuss, the paper proposes to subvert and override existing property rights of plan members.

In this paper where the employer has legal "entitlement" it's a go - where the employee has entitlement it's a no.

Our strong advice to the Government is not to go down the legal ownership road. It is a one-way trip to the Court House, and a return to endless litigation which characterized the pre-regulation era before the present Pension Benefits Act was passed.

We propose a model of pension surplus regulation that places a maximum reliance on negotiated solutions based on mutual consent and compromise between plan sponsors and plan members. There is no substitute for a reliance on creative and flexible case by case negotiation.

1. Consent

We find the paper confusing and somewhat incoherent on the critical subject of consent.

On the one hand there is a strong declaration of principle on page 13 to the effect that *all surplus withdrawals* would require the consent of the bargaining agent, or, where there is no bargaining agent, two-thirds of all plan members, as well as provisions, not spelled out, for involvement of former plan members.

Obviously, we would be very supportive of this consent provision in principle. In fact we insist upon it. The requirement that, in each and every case of surplus withdrawal, there must be consent from the bargaining agent or, where there is no union, from the plan members, is an absolute imperative.

The confusion arises elsewhere in the paper, when this principled position seems repeatedly to change. On page 5, the paper proposes that *"If an employer is clearly entitled to surplus on the basis of plan documents, the employer would be able to withdraw it with the approval of the Superintendent but without the consent of members and former members."*

Then on pages 9 and 10, the section on surplus withdrawal from ongoing plans, the paper is completely silent on the issue of consent. But it states that surplus withdrawal from ongoing plans would be permitted *"in the same manner as permitted from plans on wind-up"*, with provision for a contingency reserve.

That would seem to mean that an employer "who is clearly entitled to surplus on the basis of plan documents" could expropriate "surplus" from ongoing plans with the approval of the Superintendent but without the consent of the bargaining agent or the members of the plan.

This is precisely the situation whereby Conrad Black and Dominion stores attempted to loot $50 million from the Dominion Stores pension plan. It was the Ontario Pension Regulator who declared the Employer had clear entitlement and approved the surplus expropriation. It was the Court which ruled against the deal, criticizing the Pension Commission of Ontario for failing in its fiduciary duty to the members of the plan, opening the door to a negotiation which shared the surplus with the plan membership.

We take the position that the only valid determination as to whether or not an employer is "clearly entitled to surplus on the basis of plan documents" involves a declaration of

legal ownership which can be made by the Court and the Court alone. We assure the Government and the Employer community that any surplus regime which attempts to side-step the consent of plan members or their representatives will generate litigation in each and every case. We will require the Court and the Court alone to make the determination of legal ownership and issue the declaration of surplus entitlement in any case where our consent is withheld or sidestepped.

There is a further contradiction in the section on full plan wind-up, as set out on page 5, as well as in the consent provision set out in the proposal for partial wind-ups on page 7. There is no reference in either section to the consent of the bargaining agent. The recommendation is for *"the requisite level of consent of plan members and former members."* But the phrase found on page 13 in the section on Consent for Withdrawals is completely different. There it reads *"Amend the PBA to require the consent of the bargaining agent of plan members or, if there is no collective bargaining agent, from at least two-thirds of plan members for all surplus withdrawals,(including full wind ups, partial wind ups, and from continuing plans."*

Our question is, which is it? Full mutual consent or unilateral employer withdrawal without consent?

In principle, we accept the statement on page 13 as fair and balanced, understanding that the consent requirement will apply to each and every application for surplus withdrawal, without exception. We will not accept anything less than that. The Government must be aware that anything less than absolute consent will result in litigation on a case by case basis. And it is our clear belief that the law is on our side. If the Government is serious about its stated goal of minimizing expensive win/lose litigation, it will legislate a regime based upon negotiation and mutual consent. This creates a dynamic where the two parties can negotiate mutually advantageous solutions. This is a far more sensible approach than forcing the parties back to the Courts to fight out the question of legal ownership. We could of course make the argument that, as a result of the Schmidt case, employees have the upper hand in terms of ownership rights to pension surplus and that we could legitimately demand the right to initiate applications to use plan surplus for the enhancement of plan benefits. But we would far refer a system that facilitates constructive negotiation and mutually agreeable solutions.

With respect to the proposed change in the consent threshold for surplus distribution from ongoing plans, from 100 % to two-thirds of plan members, we have grave reservations, which we discuss below.

In cases where there is more than one bargaining agent, the consent of all bargaining agents must be a prerequisite.

Recommendation 1.
Consent of must be required in all applications for surplus withdrawal, without exception.

Recommendation 2.
In all cases where there is a trade union and a collective agreement, the Act must recognize that the bargaining agent has the responsibility and legitimacy to represent the members of the plan who are members of the union, and the consent of the bargaining agent should be the consent provision for all applications for surplus distribution.

Recommendation 3.
An application for surplus withdrawal on a full wind up, a partial wind up or a contribution holiday should require the consent of the bargaining agent, or agents, where there is a trade union, or, if there is no bargaining agent, from at least two-thirds of plan members.

2. Surplus from Ongoing Plans

We would be totally opposed to any proposal which would empower employers to take surplus funds from ongoing pension plans or from pension plans on wind up on a unilaterally basis**.** This would be a bald attempt to subvert the decisions of the Court as set out in the leading case *Schmidt vs Air Products of Canada* which established the ownership rights of pension plans members to the funds in pension plans where the plan has been established as a pension trust**.** The Court has ruled that employers have absolutely no rights to expropriate funds which are held in pension fund trusts. We estimate that between 80 and 90 per cent of defined benefit pension plans have been established as pension trusts . In all of these plans, the law has guaranteed the vested property rights of Ontario employees against attempts by employers to expropriate their property.

Such a proposal would be an affront to the stated goal of balance between plan sponsors and plan members. Aside from Multi-Employer plans, virtually all defined benefit plans are governed exclusively by the plan sponsor who is also the employer. The imbalance of power is aggravated by the systemic conflict of interest in the pension sector, where it is routine for pension actuaries to work as actuaries for a pension plan and at one and

the same time as agents of the employer during collective bargaining against the representatives of the members of the same pension plan. We have addressed this outrageous situation in previous submissions, so far to no avail.

It is worth pointing out that in any situation where an employer/plan sponsor attempts to withdraw "surplus" in ongoing plans, the plan members are totally at a disadvantage. The employer/plan sponsor is in total control of the process. The employer can create a "surplus" through his control of the actuarial process, and would have total control of the timing for filing withdrawal applications and the timing of taking gains. Employees cannot create a surplus. Nor would they be empowered under the proposal to initiate a withdrawal.

We take the view that there is no such thing as an actuarial "surplus" which can be unilaterally expropriated by the employer in an ongoing pension plan. The Court has already ruled that this is the reality where a pension trust has been established. In a pension trust, all funds are held in a fiduciary capacity for the sole benefit of the members of the trust i.e. the pension plan. This is a sound principle which should apply to insured pension plans as well. Many pension plans are still lacking in adequate inflation protection provisions. The proposal to allow employer- driven surplus expropriation from ongoing plans will simply foreclose the possibility of future benefit improvements which could and should be financed by successful pension fund investments.

One of the stated goals of the proposed changes is security. Allowing unilateral surplus expropriation at the sole discretion and initiative of the employer is an invitation to future solvency problems. Firstly, there is absolutely nothing in the history of Pension Regulation in this Province which would justify giving employers such open access to other peoples' property. Secondly, today's surplus can turn into tomorrow's deficiency in the twinkling of an eye. Ongoing pension plans must not be used as cash cows for plan sponsors.

We are therefore opposed to the proposal in the paper to lower the consent threshold for surplus withdrawals from continuing plans. It was set at the present level in the Regulation to protect the security of pension plans. We can predict with certainty that there will be a very strong reaction from the members of pension plans if this security is jeopardized.

On the issue of a buffer to protect the security of plans in the case of surplus withdrawal, we understand the Consultation proposal to weaken the existing buffer from 125% of wind up liabilities to 115%. This flies in the face of the committed goal of security and we oppose any reduction in this area.

Recommendation 4.
The consent provision for surplus distribution in ongoing plans should be the consent of the bargaining agent, or, where there is no union, 100% of the members of the plan.

Recommendation 5.
Contingency reserves in continuing plans be maintained at 125% of the plans' wind up liabilities.

3. Contribution Holidays

We are opposed to the Consultation Paper's proposal to strengthen employer entitlement to contribution holidays. At the present time, as a result of the Schmidt case, the law allows employers to take a contribution holiday unless the pension contribution requirement is based on a fixed formula with no discretion including actuarial discretion. The Government proposal would strengthen the employer's ability to take contribution holidays by allowing contribution holidays whenever a plan has a surplus unless the plan expressly states otherwise. This proposal is clearly an attempt to allow wide open surplus withdrawal in the form of contribution holidays with no restraint and with no requirement for consent.

There is no real or practical difference between a surplus withdrawal from a continuing plan and a contribution holiday. Both initiatives effectively take funds out of a plan, in the one instance pro actively and in the other retroactively. We do not feel therefore that a contribution holiday should be treated any differently from a surplus withdrawal from an ongoing plan. In other words, there must be a consent model that is exactly the same as the consent model for surplus withdrawals. There must be an actuarial buffer which protects the plan down to the buffer level.(see recommendation 5 above). And there must be full disclosure to the plan members and their agents.

This proposal to allow Employers to take contribution holidays "*unless expressly stated otherwise*" is going to be very problematic. What does this phrase mean? Does it mean that, in a matching contribution plan based on a fixed formula, where contribution holidays are now prohibited, they will be permitted in the absence of an expressed prohibition? This will fundamentally change the nature of such a plan, in which

contribution holidays were never contemplated. In plans where the contribution formula is set out in the collective agreement, this proposal will override and nullify the collective agreement. It is simply unacceptable that the PBA be amended in such a way as to override the provisions of collective agreements for the one-sided benefit of employers. Again, this is an affront to the stated goal of balance.

There is only one way to resolve pension surplus issues rationally and sensibly and that is through negotiation based mutual consent. Anything else will carry us back to win-lose litigation in Court. Perhaps the Employer community has forgotten how nasty and costly that can be, not to mention the very strong rights which have been endowed on plan members by the Court. But the Government would be well advised to remember.

Recommendation 6.
Contribution holidays should only be permitted on basis of the consent of the bargaining agent, or, the consent of two thirds of the members of the plan.

Recommendation 7.
Applications for contribution holidays should be subject to the same actuarial buffer that protects on going plans.

4. Wind Ups

Once again, in the case of wind ups, we warn against trying to solve issues of surplus distribution on the basis of asserted legal ownership by Employers rather than by negotiation based on mutual consent.

The problem with the ownership model is that every claim to ownership has to be tested in Court. There should not be any exceptions to the consent principle set out on page 13 of the paper, but apparently abrogated on page 5 and elsewhere in the text.

We appreciate that at least some of the impetus for the proposed changes comes from recent Court cases.

In the Tecsyn case, the Court has clarified that the language of section 79(3) the PBA prevails over the language of the Regulation, and that there can be no payment to an employer unless the employer has legal ownership of the pension surplus in question. The problem with the Government's proposed solution, which relies on the model of legal ownership, is that "ownership" has to be proved in Court. As long as ownership

rather than consent is used as a basis for surplus withdrawal, dissidents will be able to stop deals they oppose through litigation. The prudent course is to remove all references to ownership from the PBA and enact provisions that allow the parties to reach settlements based on mutual consent. There is no other way to fix the problem caused by the Tecsyn case. The Paper's proposal is a guarantee of endless litigation that will actually impede the process of surplus sharing.

In the Monsanto case, the paper seems to take a position in opposition to the position taken by the Pension Regulator and the Financial Services Commission! We should not have to remind the Ministry that in the Monsanto case the Court upheld the Governments' position, that partial wind ups should be treated the same as full wind ups and surplus must be distributed to the plan members. The paper's suggestion, that surplus distribution on partial wind up be at the employer's option, and that, instead of a surplus distribution on partial wind up, some kind of list be maintained for a future distribution at full wind up, is in our view totally impossible to accomplish. It would be impossible to calculate the attribution of surplus entitlement to the members on the list, assuming that the list could be properly maintained. The effect will be to wipe out and eradicate the vested pension rights of the plan members affected by the partial wind up. This is an intolerable proposal. The basic principle must be that employees on a partial wind up are entitled to the same rights as employees on a full wind up. In both circumstances, surplus distribution must be mandatory, and the consent principle must apply.

Recommendation 8.
Our position in the case of partial wind up is that surplus distribution should be mandatory, and that the wind up proposal should have the consent of the bargaining agent, or, two thirds of the plan members.

Recommendation 9.
We support the proposal for mandatory surplus distribution on full wind up.

5. Surplus Attribution

On the matter of surplus attribution, we support the proposal to abolish surplus attribution analysis. We do suggest that a straightforward history of pension contributions would be very useful. A history of the flow of funds into and out of a pension plan should be a requirement.

Recommendation 10.
We support the proposal to abolish surplus attribution analysis.

6. Arbitration

The OFL supports an arbitration system for the resolution of disputes. An arbitration regime is an obvious adjunct to our preferred model of negotiation based on consent.

But we have concerns about the very limited role assigned to the arbitration model proposed in the paper. Firstly, it is totally unbalanced and biased in the Employer's favor. The Paper proposes only Employer initiated arbitration, where the Employer gets the support of fifty percent of the plan members but not the requisite two-thirds. So the plan members do not have rights granted the Employer to initiate an arbitration.

It is inconceivable that such a lop sided proposal would be enacted.

And once again, the page 13 consent position which requires the consent of the bargaining agent has once again fallen off the table and disappeared. Again, we must insist that there be one set of consent rules, not four or five.

The provision for a threshold of 50 % of the members who vote is unacceptably low. It is totally out of sync with other Canadian arbitration regimes. And it provides a real

incentive for employers to low ball their distribution offer and go to arbitration. There is no mention of time limitations, and in all pension matters, time is on the side of the employer. An arbitration could last a number of years, there could be a new valuation, the surplus could be gone.

Finally there is the serious issue of the criteria which will govern the arbitration process. What is being proposed is simply a yes or no to the Employers' proposal, presumably, once again, on the basis mainly of an adjudication of legal entitlement. The factors set out for discussion on page 15 are incomplete. We propose that the new arbitration regime be based on considerations of equity. Other factors which must be taken into account would include the level of benefits in the plan, the impact of inflation erosion on members' benefits, and the degree of equity between plan members.

A genuinely balanced arbitration regime would also permit plan members to initiate an arbitration proceeding, assuming of course that equity factors were part of the arbitration process.

Recommendation 11.
The arbitration process must give balanced rights of access to both plan sponsors and plan members, and must be based on factors that include considerations of equity.

We believe that the recommendations proposed in this brief would go a long way to resolving the issues related to pension surplus distribution.

Representatives of the OFL pension have been serving in an advisory capacity to the Financial Services Commission of Ontario for a number of years and we would be pleased to discuss these issues with representatives of the Government prior to the introduction of legislative amendments to the Pension Benefits Act.

Respectfully Submitted.

Ontario Federation of Labour

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