



A **Biggger** PIE

By *H. Clare Pitcher*

Why MEPPs and TBPs are the way of the future to increase pension coverage

Currently, only four out of every 10 Canadians are covered by a pension plan other than the Canada Pension Plan or Quebec Pension Plan. Employers often don't like DB plans because they're too risky. Employees will take anything they can get but would normally prefer DB plans. How do we resolve this conflict and increase pension plan coverage in Canada?

Multi-employer pension plans (MEPPs) have been around since the middle of the 20th century. Typically, they are target benefit plans (TBPs) that involve a union or unions. More recently, a renewed breed of MEPP/TBP has been conceived by each of the key expert pension commissions across the country (Alberta/B.C., Ontario, Nova Scotia and federal). They simply referred to them by slightly different names: SCTBP (specified contribution target benefit plan), JGTBP (jointly governed target benefit plan), TBP (target benefit plan) and NCDPB (negotiated cost defined benefit plan), respectively.

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Understanding MEPPs and TBPs

Traditional MEPPs—or, more specifically, SMEPPs (specified multi-employer pension plans), to differentiate them from public sector DB MEPPs:

- involve several participating employers;
- are union-negotiated/collectively bargained;
- are governed by joint labour-management or 100% union-trusted board;
- are structured as a combination DB/DC plan, with both benefits and contributions defined (the objective is DB, but the promise is DC);
- have fixed contributions (typically a cents-per-hour defined contribution rate) that go into the plan on a DC basis, and benefits (typically flat dollar) that are paid out from the plan on a DB basis;
- have benefits that are targeted and are paid as scheduled, contingent on the plan's financial position;
- require members to bear 100% of the risk on a collective basis; and
- are "specified" as per the federal *Income Tax Act*.

MEPPs have weathered the financial storms of the past half-century, including

the perfect storm of the early 2000s and the economic and market crisis of 2008. While benefits in most MEPPs have been reduced, on either or both an accrued past service and future service basis, it is likely that these reductions are only temporary and will eventually be restored as markets and economies recover. These plans are designed to weather the volatility of our times—something that traditional DB and DC plans struggle with.

TBPs will need to share many fundamental features with MEPPs in order to be effective:

- trustees have the ability to reduce accrued benefits;
- the employers' liability is limited to the fixed negotiated or agreed-upon contributions;
- the plan is viewed as DC for both accounting (CICA, IFRS) and tax [Canada Revenue Agency (CRA)] purposes; and
- there is no solvency funding requirement.

But the TBP concept envisioned by the expert commissions goes beyond the traditional MEPP in that there may be only a single employer or corporation, there may not be a union involved, and the contribution and benefit formulas are not limited to cents-per-hour and flat benefits, respectively (i.e., they may also be formularized as a percent of salary).

The Future of TBPs

What has to happen in order for TBPs to flourish across the country? First of all, TBPs need to be formally recognized in the various provincial legislations and

regulations. This has already started to happen in Ontario, where *TBP* has been defined under the *Pension Benefits Act* (PBA) and the MEPP/TBP concept clarified with respect to single employers. The part of the proposed new law referencing the union versus non-union aspect uses the term "collective agreement." Simply removing the word *collective* would open up the TBP design to the huge Ontario private sector non-union environment.

The various provincial PBAs, the federal *Pension Benefit Standards Act* and the associated regulations, while viewing these plans as fundamentally DB, must allow the reduction in accrued benefits (just as Ontario's does for MEPPs); exempt these plans from solvency funding (just as Ontario's does for specified Ontario MEPPs and in line with new permanent exempting legislation now on the books); and not require the employer to make up any deficit in the plan. This is not the case in Quebec and New Brunswick, where MEPPs—and presumably the new TBPs—simply do not and will not work well because of the funding risk and associated DB accounting.

In addition, the provinces must extend the TBP to the single-employer and non-union environments. The federal taxation authority (the CRA) must view these TBPs as DC plans, just as they do SMEPPs—and, like the provinces, extend the application to the single-employer and non-union environments. Finally, the accounting authorities (CICA and IFRS) must view these plans as DC plans, just as they do SMEPPs, on the basis that the employer's liability is limited to the fixed contribution rate.

Assuming that this legislative and regulatory environment is put in place, the stage is set for unprecedented growth in registered pension plans, extending private pension plan coverage beyond the existing four out of 10 Canadian workers to the remaining six out of 10 employees—the fundamental objective of the various expert pension commissions.

A "Perfect" Solution in an Imperfect World

In a perfect world, employers would prefer DC and most employees would prefer DB. But in our "real" world,

employers would prefer TBPs over DB plans because they have...

- no surplus/deficit asymmetry and ownership issues (surpluses and deficits are 100% the members' responsibility);
- no solvency funding requirements, other than calculation and disclosure;
- predictable fixed costs/contributions;
- no accounting problems or complexities or unforeseen hits to the employer's financials;
- transfers of risk and the associated responsibility of benefits/deficits to the members;
- simpler and more flexible taxation rules (e.g., DB excess surplus rules are not applicable, pension adjustment calculations are simple); and
- ease of administration advantages (the burden is transferred to a board of trustees and expenses are charged to the fund).

Again, in our real world, employees would prefer TBPs over DC plans because they have...

- sharing or pooling of investment and mortality/longevity risks;
- more secure and predictable benefits determined by a set scale or formula;
- economies of scale (i.e., lower expense unit costs);
- access to DB-type pension ancillaries, such as disability and subsidized early retirement benefits;
- better investment returns, producing

significantly higher pensions; and

- joint governance.

MEPPs/TBPs represent a practical alternative to a traditional DB or DC plan that optimally balances the often-conflicting needs and objectives of both employers and employees, taking the best of both DB and DC worlds.

From the member's perspective, the TBP has all of the features of a DB plan, except that it is contingent on the plan's success. From the employer's perspective, the TBP functions like a DC plan, with no obligation to fund deficits or beyond the fixed agreed-upon contributions.


Governance for these new TBPs will be critically important. Given that the risk is borne by the members, at a minimum, the employees must have a 50%—possibly even 100%—share of the governance.

Jointly governed TBPs will likely become the norm, with basic current service cost (i.e., not including any deficit funding requirement) sharing anywhere from 100% employer/0% employee to 50/50. In this new world of operating a MEPP/TBP in a non-union situation, the traditional role of the union representatives acting as trustees will be met by member association or employee-elected representatives to a pension committee or board of trustees.

Finally, assuming that the necessary legislative and regulatory changes are made, we will have a plan design—the TBP design—which effectively works for

both employers and employees in the private sector. This sets the stage for increasing the pie of registered pension plan coverage. With an effective vehicle that meets the two major stakeholders' requirements, pension plan coverage could be further enhanced by making a registered pension plan a mandatory requirement for all employers (or at least those meeting a certain size threshold, such as a minimum of 15 employees).

Opening up access to private pension plans via the TBP for the remaining 60% of Canadian workers will cost nothing to the government or taxpayers, as there is no Pension Benefits Guarantee Fund safety net. In fact, the ultimate beneficiary—along with the newly covered employees themselves—will be future taxpayers, as the potential need for government social assistance down the road will be reduced significantly.

What's needed now is to take this "new" plan design from the point of conception to the actual birth of the new TBP for use in the single- as well as multi-employer environment—and in the non-union as well as union environment—thereby increasing the pie and broadening pension plan coverage across the province and the country. 

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