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AT A GLANCE ...

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employee benefits specialists

Market meltdown ignites pension solvency turmoil

The year 2008 will be remembered as the year of the worst equity market since 1929 as markets around the world reacted to the collapse of the US housing market and the near bankruptcy of some of the world's leading financial institutions.

In the months of September and October, equity markets lost over 20 per cent of their value, straining the asset bases of everything from pension plans to banks to insurance companies.

In the US alone, almost $3 trillion was lost due to the credit crisis, according to the US Congressional Budget Office. In Canada, more than $100 billion in equity value disappeared in less than six weeks. Comparable losses were experienced throughout the European and Asian markets, forcing governments to loosen credit and direct billions of dollars to support their failing financial institutions.

Meanwhile, pension plan funding ratios of assets-to-liabilities dropped to a record 72 per cent, spreading alarm throughout the government and financial services sectors.

Outside of private investors who rely on equities to fund their group and individual registered retirement savings plans, the first major casualties of the equity crisis could be Canada's 1,400 federally regulated pension plans, according to national pension experts.

Actuaries urge federal intervention

The Canadian Institute of Actuaries (CIA) warns that plan sponsors across the country could face bankruptcy unless the rules governing pension plan solvency requirements are eased.

According to CIA Board Member Jacques Lafrance, employers could face a financial crisis as early as this December as they will be expected to make up any shortfall in their pension plans. According to Mr. Lafrance, up to 70 per cent of pensions are probably underfunded, thanks in part to the asset losses resulting from this autumn's market meltdown. With an uncertain economy and tightening credit, many plan sponsors will be unable to make up the funding shortfall using traditional funding mechanisms.

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The 2008 meltdown in numbers:

-30%: The loss on the Toronto Stock Exchange and New York Stock Exchange from September 15 to October 30.

-20%: Estimated pension fund losses year-to-date.

72%: Estimated average solvency ratio of Canadian federally regulated pensions, the lowest on record. Previous record: 77 per cent.

70%: Estimated percentage of pension plans that are underfunded.

$100 billion: Canadian equity value lost in the six-week market decline.

How much?

Pension deficits of selected Canadian organizations:

Air Canada:	**$1.2 billion**
Nortel Networks:	**$1.1 billion**
BCE:	**$449 million**
University of Waterloo:	**$50 million**

(Sources: *The Globe and Mail* and *The Toronto Star,* October 30, 2008)

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For some plan sponsors, the year-end 2008 valuations will reveal the need for "huge" contribution increases, according to the CIA. The result could mean bankruptcy for some organizations, he suggests.

"Under federal regulations, if your pension is underfunded, you must file every year a new actuarial valuation with the federal government. The concern is that when these companies file their valuation, it will reveal a significant increase in their deficit," he says.

While specific contribution increases will vary by plan sponsor, published reports in major newspapers quote pension actuaries as estimating that contribution increases of 100 to 200 per cent may be required by some plans to meet their solvency requirements. Some plan sponsors may simply not be able to meet that commitment.

"If an employer goes bankrupt and there is a deficit in the pension plan, benefits of all plan members will be reduced, including retirees," says Mr. Lafrance. "If you are a politician, you need to be aware of these risks. If you don't do anything, the current situation may precipitate bankruptcies."

Various options on the table

According to the CIA, the federal government may have to reduce the minimum funding requirements of pension plans and segregated funds. Suggestions also include providing letters of credit, or loan guarantees, to allow plan sponsors to borrow funds to shore-up their pension solvency requirements.

There is precedent for providing loan guarantees to pensions under stress. In 2004, government loans and guarantees helped failing Stelco to protect its pension after it reported a deficit of $1.3 billion. However, at that time, the government didn't face a system-wide pension solvency issue and a worldwide banking crisis.

Suggestions by the Canadian Association of Pension Management (CAPM) and the Canadian Chamber of Commerce include extending the time requirement for plan sponsors to make up funding shortfalls from the current limit of five years to 10 to 15 years. This will give pension plan administrators an opportunity to take advantage of the economic cycle and the economic recovery that will ultimately occur in the future.

"All we're saying to the government is give us more time to take care of this," says CAPM President Scott Perkin.

However, since many of those plan sponsors were lax in topping up their pensions' funding when equity markets flourished from 2004 to 2008, providing them with extra room to postpone their pension solvency commitments may not be acceptable to retiree groups, consumers or some labour organizations.

Another suggested option is postponing the December 2008 valuation to a later date.

However, this too could result in a deferral of plan sponsor obligations to top up their pensions and, ultimately, earn the anger of consumer and labour groups.

"This is the opposite of what pensioners have demanded," says Canadian Association of Retired Persons (CARP) Vice-President, Advocacy Susan Eng. *"Now, their pensions are even more at risk."*

In the meantime, Federal Finance Minister Jim Flaherty says the government is considering its options. An announcement is expected in the near future.

Change conversion rules, premiers urge

Two provincial premiers have urged the federal government to change the income conversion rules governing registered retirement savings plans (RRSPs).

Manitoba Premier Gary Doer and Nova Scotia Premier Rodney MacDonald have both urged the government to loosen the requirement that registered plans be converted to retirement income funds at age 71.

According to the two premiers, seniors across Canada could lose thousands of dollars in retirement savings if they are forced to convert their funds following this past autumn's market collapse.

"If we don't get it right on pension plan flexibility, we could have the market just whack a lot of people close to age 71 and they may take a huge hit," Mr. Doer said on November 10.

Mr. MacDonald echoed the Manitoba premier and suggested that the mandatory conversion age be extended to age 75 to allow time for equity-based retirement savings plans to recover from this fall's market turmoil.

"Otherwise, we could see many seniors losing thousands of dollars," he stressed.

The premiers' suggestions parallel those of the Canadian Association of Retired Persons (CARP), which extended the suggestion to allow seniors to also delay making withdrawals from registered retirement income funds (RRIFs) until their assets can recover from the market crash.

Under the current rules, RRIF policyholders are required to make a minimum withdrawal from their retirement funds every year. Many of those funds experienced significant losses this past autumn.

However, CARP wants the conversion delay to be extended permanently.

"CARP has been on record suggesting that they do this permanently, not just in a market downturn," says Susan Eng, the organization's vice-president of advocacy.

The CARP proposal has also received support from conservative policy groups such as the CD Howe Institute.

"Seniors are forced to make the withdrawals whether or not they make sense," says the Institute's William Robson. *"Since 1992, when changes to the Income Tax Act last adjusted the minimum withdrawals, life expectancy is up and real returns are down. As a result, seniors face a dramatic erosion in the purchasing power of tax-deferred savings in their later years. The required minimum withdrawals should fall or disappear."* ❧

BC to launch its own pension plan

The province of British Columbia says it will develop its own pension plan for workers who do not have access to pensions at their workplace.

Premier Gordon Campbell says the new plan will be a voluntary, defined contribution arrangement that will be open to all employers, employees and self-employed people. The government hopes to pool pension contributions to create one viable, guaranteed plan for those who do not have guaranteed pension entitlements.

Approximately 75 per cent of private sector workers in BC are not covered by a group pension plan.

A similar scheme is under review by the Nova Scotia Pension Review Panel. ❧

OSFI requires trustees to disclose their power to reduce benefits

The Office of the Superintendent of Financial Institutions (OSFI) has issued a guidance note to boards of federally regulated multi-employer pension plans requiring them to disclose to their plan members their power to cut or reduce pension payments and credits.

In its September 29, 2008 note, OSFI states that where plan or trust agreements, or any other documentation, permit trustees to reduce accrued pension credits and benefits, plan trustees must communicate that they have this authority to all plan members, former members and participating employers.

Employee groups to be covered in the communiqué include:

- active members at the time of their enrolment in the pension plan;
- retired and deferred vested members;
- former members, their spouses and beneficiaries; and
- active members and their spouses at their retirement or termination with a deferred pension benefit.

Communication vehicles must include annual plan statements and booklets, OSFI says. ❧

Nova Scotia public pension faces rate hike or benefit cuts

Nova Scotia's civil servants will either have to accept decreased benefits or pay larger premiums, says provincial Finance Minister Michael Baker.

The minister was reacting to a report by that province's pension agency stating that the provincial pension plan has an unfunded liability of more than $912 million.

Membership in the province's defined benefit plan exceeds 28,600 people.

"There are only three ways to improve the plan: increased contributions by members and the government, changes to benefits or better market performance," he said. *"The last of those three methods seems to be far fetched at the moment. That leaves us with the other two as the only options."*

The minister ruled out adding more government money to the pension, outside of the 50 per cent funding it already provides.

"We are responsible for 50 per cent of the contributions to the plan. Our commitment to that is strong. But, there are no plans that would see taxpayers putting more money into this plan," he said.

According to pension advisory board trustees, the plan lost between $300 million and $400 million since April 1 of this year. ❧

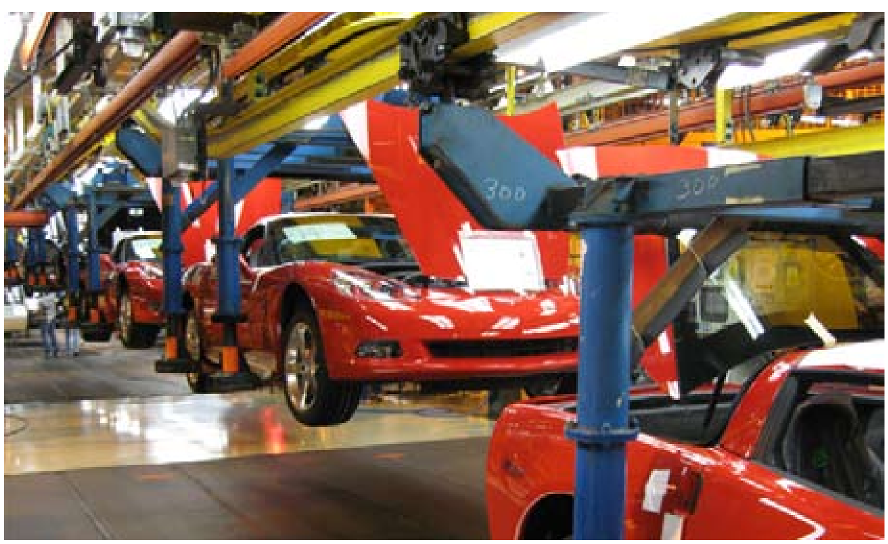
GM suspends some benefits

General Motors' US operations announced that it suspended certain benefit programs, effective November 1, 2008.

As part of its effort to address its multi-billion dollar losses brought on by plummeting auto sales, the company has discontinued its tuition reimbursement and adoption assistance programs. Plus, it will no longer match employee contributions to 401 (k) retirement savings programs, which are similar to registered retirement savings plans (RRSPs) in Canada.

The company says it will also eliminate health care benefits for salaried retirees over the age of 65.

The cuts do not apply to the company's Canadian operations. ❧



OSC seeks pension disclosure records

The Ontario Securities Commission (OSC) has entered into the 2008 market meltdown debate by asking major Canadian companies to review their pension plans and provide details on them to their directors and investors.

In a letter sent to some of Canada's largest plan sponsors, the OSC asks companies to ensure that they comply with their fiduciary responsibilities to disclose information about their pensions to existing and potential investors.

"Given the current economic conditions, we are currently reviewing pension disclosures for companies with defined benefit plans," the OSC says.

A response to the OSC must also be sent to the various plan sponsors' audit committees and to their external auditors.

While the OSC is Canada's premier securities regulator, it has no jurisdiction over pensions. However, its entry into the pensions arena illustrates the depth of the pension undervaluation problem, which could potentially sink the value of plan sponsors' equities should they be unable to meet their pension funding obligations.

According to reports published in the November 14, 2008 edition of *The Globe and Mail,* the OSC is responding to public concerns about the deterioration in pension funding and to the growing speculation on the impact the pension funding problem will have on various companies.

While companies are not required to respond to the OSC letter, the securities regulator promises that it will continue to monitor companies and/or review their disclosure records to ensure they meet their governance requirements. ❧

Health care spending to top $171 billion

Health care costs in Canada will exceed $171 billion this year, the Canadian Institute for Health Information (CIHI) says.

According to the health information agency, spending for health care now averages $5,170 per person annually and accounts for 10.7 per cent of Canada's gross domestic product. That average amount per person is a dramatic increase from the $3,678 reported in 2006 and will move Canada to second place in per capita health care spending. The US leads the world in health care spending at a reported $6,714 per person in 2006.

The three largest components for health care expenditure are hospitals, pharmaceuticals and payments to physicians. The total costs, percentage of health care expenditure and cost growth rate are:

Area	Total costs	Per cent of health care expense	Growth rate
Hospitals	$48.1 billion	28.0%	5.8%
Pharmaceuticals	$29.8 billion	17.4%	8.3%
Physicians	$23.0 billion	13.4%	6.2%

Most dangerous occupations have lowest literacy rates

A Conference Board of Canada study suggests that 40 per cent of workers do not have the literacy skills to do their jobs safely. Ironically, those industries with the highest requirements for health and safety tend to have the lowest investment levels in employee literacy training, the Conference Board says.

According to its survey, the construction, transportation and utilities industries spend less than $4 per employee on literacy training compared to the $13 and $32 spent respectively by the far less dangerous financial services and communications technology industries.

"Low literacy skills do more than just threaten an organization's productivity and competitiveness, they also put workers' health and safety at risk," a Conference Board spokesperson said. ❧

CAPSA releases multi-jurisdiction rule update

Canada's pension supervisors are proposing new regulatory standards for pensions involving more than one jurisdiction.

In an October 21, 2008 policy paper, the Canadian Association of Pension Supervisory Authorities (CAPSA) introduced a series of proposals to clarify what rules would apply when a pension plan covers members in more than one province.

The new rules would continue to distinguish between the jurisdictions of the *"major authority"*, the province where the *"plurality"* of plan members are employed and where the plan is registered and the *"minor authorities"*, the other jurisdictions where plan members may be employed.

Items under consideration include the following:

1. Matters affecting a pension as a whole be governed by the major authority while members' pension entitlements be governed by their individual jurisdiction. As well, funding rules of the major jurisdiction would apply across the entire pension plan.
2. The major authority will be required to supervise and regulate the pension plan on behalf of all the other minor authorities. This includes enforcement of regulatory, governance and other statutes.
3. Initial decisions on any matter be made by the major authority, based on its pension legislation. Any legal recourse arising from those decisions be settled in the major authority. However, member entitlement issues should be settled in the relevant minor authority, based on its laws.
4. The final calculation of member pension income entitlements be based on the jurisdiction where the member is located at the time pension benefit is determined. ❧

DI programs need harmonization

Canadian disability income programs need harmonization, says the Institute for Work & Health.

In a September 2008 report entitled *Disability Income Security Benefits for Working-Age Canadians,* the Institute describes Canada's disability income (DI) support system as an unco-ordinated patchwork of federal, provincial and private programs that often work at odds against each other.

In its review of the Canada Pension Plan (CPP), provincial workplace compensation, provincial social assistance and private long-term disability plans, the Institute says current DI programs suffer from "massive bureaucracy", especially when claimants qualify for benefits from more than one program.

"Over time, we have created a system that imposes on people a very difficult administrative process," says Institute President Cam Mustard. *"The only reason it's there is that we've allowed it to go this far."*

One area cited by the Institute's report is the widely different disability income payments that may be provided to workers even when their incomes and injuries may be identical. This, says the Institute, is partly a result of the different eligibility criteria used by the disability income plans. For example, provincial compensation programs have an application denial rate of five per cent while the CPP disability plan has a denial rate that exceeds 30 per cent.

"The criteria to qualify for that [the CPP] benefit are quite stringent," Mr. Mustard says. *"An applicant has to demonstrate that he or she will never work again while the perspective of the provincial workers' compensation and private employee benefits plans is that people will work again."*

The first step toward harmonization should be the establishment of a common definition of *disability,* he asserts.

"The great tragedy of this is that the last thing you want to do as a society is to bring a huge administrative challenge onto someone who is going through a very scary experience," he says. ❧

Sun, surf and scalpel

Medical tourism has become the latest benefit offered by some US plan sponsors.

In an effort to reduce medical plan expenses, some plan sponsors are offering to cover their employees' travel and medical expenses for overseas medical treatment, including major surgery.

With procedures such as open heart surgery costing up to $100,000 in the US, many plan sponsors and insurers find that paying for both travel and associated medical expenses in countries such as Singapore, India, Costa Rica, the Czech Republic and others are much cheaper than using American-based medical facilities. For example, the cost of open heart surgery in India amounts to $8,500, more than enough to pay for a member's additional accommodation and return travel expenses when compared to the cost of surgery in the US. Similar savings are available for hip and knee replacements and other surgery. Plus, many foreign hospitals have North American or European-trained physicians and surgeons on staff.

The medical tourism benefit can also provide an alternative to high plan deductibles, which can amount to as much as $10,000 in some medical plans. For example, relatively minor surgery such as hernia operations cost approximately $13,000 in the US compared to $3,900 in Costa Rica. Medical tourism can help reduce out-of-pocket expenses for plan members facing such procedures.

A Deloitte study indicates that, in 2007, as many as 750,000 US patients travelled abroad for medical services, including cosmetic and dental surgery. ❧

Fast facts

- Statistics Canada reports that the percentage of workers receiving non-wage benefits jumped from 67 per cent of the workforce in 1999 to 74 per cent in 2005. The government agency also says that more plan sponsors now offer at least one non-wage benefit, with the number rising from 41.8 per cent to 48 per cent of workplaces from 1999 to 2005.

  The situation is the reverse in the United States, according to the US Economic Policy Institute. The number of American workers receiving benefits has declined from 68 per cent in 2000 to 63 per cent today.

- The Canada Revenue Agency says the 2009 yearly maximum pensionable earnings (YMPE) level for the Canada Pension Plan will be $46,300, up from $44,900 in 2008. The contribution levels for both employers and employees remains 4.95 per cent respectively for a combined total of 9.9 per cent of pensionable income.

- Employers in Quebec must now provide unpaid leaves of absence to employees who request leaves after they or their family members have been victims of crime. Under Bill 58, employees may qualify for up to 104 weeks of unpaid absence if they, their spouse or dependant children are injured as a result of criminal activity. The law also provides 52 weeks of unpaid leave to employees whose spouses or children have committed suicide or if a child has been reported missing.

  Employers must continue to provide benefit coverage during the leave.

- A survey sponsored by the Human Resources Professionals Association says that 49 per cent of employers expect up to 40 per cent of their workforce to retire within the next five years. Only 14 per cent of surveyed employers said they were prepared to cope with the projected labour shortage.

- It takes an average of $10,000 per year to clothe, feed and keep a child healthy, according to data released by the government of Manitoba.

- The Old Age Security (OAS) benefit increased to $516.96 per month, effective October 1, 2008, a 2.2 per cent jump from the previous quarter. The increase reflects the change in the cost of living as measured by the Consumer Price Index.

- The average weekly earnings per Canadian worker as of June 1 of this year: $789.23, or $41,039.96 per year.

- While post-traumatic stress disorder (PTSD) is usually associated with soldiers returning from combat, up to one in 10 people experience PTSD in their lifetime, according to a survey of almost 3,000 people conducted by McMaster University. The unexpected death of a loved one, witnessing an injury or death and sexual assault are the most common causes of PTSD among civilians.

- The government of Argentina nationalized all private pension plans this past October. The move was in response to this autumn's collapse in equity markets. In announcing its action, the Argentine government called private pension schemes offered by that country's 10 largest plan administrators a *"failed experiment."* Critics accused the government of grabbing private funds to service its debts. ❧

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