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JOINT FORUM OF FINANCIAL MARKET REGULATORS

DISCUSSION PAPER

**“PROPOSED REGULATORY PRINCIPLES FOR
CAPITAL ACCUMULATION PLANS”**

RESPONSE BY THE ONTARIO BAR ASSOCIATION

PENSIONS AND BENEFITS SECTION

I. ONTARIO BAR ASSOCIATION, PENSION AND BENEFITS SECTION – WHO WE ARE

The Executive of the Pensions and Benefits Section of the Ontario Bar Association is pleased to provide its comments on the Discussion Paper issued by the Joint Forum of Financial Market Regulators entitled “Proposed Regulatory Principles for Capital Accumulation Plans” (the “Discussion Paper”).

The Section has approximately 350 members who practice in the pension and benefits area. The Executive consists of 14 members who practice almost exclusively in the pension area. The clients of Section members include large and small employers, trade unions, pension plan administrators, custodians, investment counsel, executive and salaried employees, deferred vested plan members and retirees.

II. GENERAL COMMENTS

At the outset, we acknowledge that there is considerable uncertainty surrounding the obligations of employers who provide, and the administrators of, CAPs and we welcome the initiatives of the Joint Forum in opening up discussions in this area with a view to clarifying the responsibilities of employers and administrators in relation to CAPs.

In particular, we note that the existing pension legislation is focused on defined benefit pension plans and does not deal adequately with defined contribution pension plans, whether they are plans in which the employer makes all of the investment decisions or they are ECDCPPs. Indeed, the existing pension legislation is silent on a number of issues that arise only in relation to defined contribution pension plans, such as, for example the allocation of responsibilities between members, plan administrator and employer in relation to investment of contributions made to the plan.

The Discussion Paper contains many suggestions that seem to have their genesis in the retail securities investment environment. There are, however, some differences between the issues faced by investors who deal with investment advisers and by members of CAPs. As a result, the nature of the protection that such investors and CAP members require is different. We submit that, the nature of these differences have not been adequately explored in the Discussion Paper. Moreover, in commenting on the proposed regulatory principles we should not be perceived as necessarily supporting the view that the securities model of regulation is the better or preferred model.

Many of the proposed regulatory principles as articulated in the Discussion Paper could raise numerous questions and potential problems for plan administrators and employers. The result in some cases could be that some plan administrators or employers would either not provide CAPs or offer prospectus qualified investments. The Joint Forum should recognize that if the latter scenario described in the previous sentence occurs, the investment management fees associated with CAPs will increase. Over time these higher investment management fees will lead to lower accumulated savings in the CAPs.

Certain of the proposed regulatory principles as articulated in the Discussion Paper would also be of concern to employees. For example, it is not clear that proposed regulatory principles would ensure that employees are provided with sufficient information regarding investments, sufficient investment options, and other relevant information and protections to ensure that they make informed investment decisions. To the extent that this information is not provided, the interests of employees will not be adequately protected under the proposed regulatory principles.

By its very nature the Discussion Paper espouses general principles and does not delve into the details. However, where the Discussion Paper does provide details, the way those details are presented raises many questions concerning what is intended. Therefore, many of our comments pose questions to help highlight the areas of uncertainty and confusion and to assist the Joint Forum in developing a more detailed revised set of proposed principles.

Our comments on the Discussion Paper are structured as follows:

We have answered the first question posed on page 33 of the Discussion Paper in Section III and IV of this response. Section III comments on inaccuracies in, or misstatements made in, the Discussion Paper. Section IV comments on issues or matters which we believe were not, and should have been, addressed in the Discussion Paper.

In Sections V-VIII we have looked at each of the four proposed regulatory principles, in turn, and answered questions 2-4 posed on pages 33-34 of the Discussion Paper in relation to each proposed regulatory principle.

We also note that the Discussion Paper indicates that it is focussing primarily on ECDCPPs and Group RRSPs and that further work may be necessary to determine whether the proposed principles are appropriate for DPSPs, EPSPs and other types of CAPs. We welcome the Joint Forum's recognition that any regulatory principles which emerge from this current project may not be appropriate for DPSPs, EPSPs and other types of CAPs. Each type of CAP has its own characteristics and therefore whatever the final principles that emerge as applicable for one type of CAP should not automatically apply to other types of CAPs.

It follows equally that all of the regulatory principles that are considered as appropriate for ECDCPPs may not be appropriate for Group RRSPs. In this regard we also note that there are two very distinct types of Group RRSP (where the employer makes a "contribution" and ones where there is no employer "contribution"). We submit that any regulatory principles that are appropriate for one kind of Group RRSP may not be appropriate for the other.

III. ERRORS AND INACCURACIES

The Discussion Paper contains some fundamental misconceptions about CAPs and the legal framework surrounding them. There are also some oversimplifications of complex issues and of the scope of the pension legislation. For example, the description of the fundamentals of pension legislation does not acknowledge that the pension legislation in various provinces operate differently in some of the specific areas discussed.

We address some of the more obvious misconceptions and oversimplifications in our comments below. We believe that it is important to draw attention to these areas to ensure that any policy initiatives that emerge out of the Discussion Paper are based upon a full, correct and accurate understanding of the current environment.

- The Discussion Paper states that CAPs are “primarily intended to ensure the financial security of the employees in their retirement”. This is not correct. CAPs do not purport to provide *any* level of financial security for employees in their retirement. At most, *some* CAPs (e.g. ECDCPPs) provide employees with a vehicle by which they can undertake tax-assisted savings for retirement. Whether the employee is financially secure in his or her retirement depends on a whole range of factors such as the level of contributions made to the CAP by the employee, the investment choices made by the employee, the economic environment when the employee retires and the specific financial needs and circumstances of an employee when he or she retires.
- The Discussion Paper defines CAPs broadly to encompass a broad range of defined contribution plans. The Discussion Paper then states that CAPs are “primarily intended to ensure the financial security of the employees in their retirement”. In addition to the comments made above, the attempt to attribute a retirement focus to *all* CAPs is too much of a generalization. While the ECDCPP has the primary purpose of providing employees with a vehicle by which they can undertake tax-assisted savings for retirement, many CAPs are established purely as a savings vehicle. For example it is difficult to characterize EPSPs as a retirement savings vehicle. Also many employers provide Group RRSPs and DPSPs with the primary purpose of providing their employees with a tax-assisted *savings* vehicle and not necessarily a *retirement* savings vehicle.
- The Discussion Paper attempts to summarize the “statutory fiduciary duty” imposed on administrators of pension plans. There are many oversimplifications in this summary. First, the statutory standard described in the Discussion Paper does not reflect the way the standard is described in all jurisdictions. Second, the Discussion Paper suggests that the statutory standard is applied to agents of the pension plan administrator. This is only true in some provinces (e.g. Ontario and British Columbia). However, in other provinces (e.g. Alberta) the pension legislation does not impose those duties on agents of the plan administrator.
- The Discussion Paper states that “plan administrators and their agents are considered fiduciaries under both pension legislation and the common law”. To the extent this comment refers to common law, we are not aware of any case which has concluded that, as a general proposition, administrators of pension plans or indeed Group RRSPs or their agents are fiduciaries in all cases. The Discussion Paper’s oversimplification on this point is particularly important in relation to Group RRSPs, since the pension legislation statutory standard of care does not apply to Group RRSPs.

- The proposed regulatory principles contemplate that the fiduciary duties of employers *and* administrators should be clarified. This suggests that employers may currently be subject to fiduciary duties in relation to pension plans. However, the current case law indicates that the employer/employee relationship does not *automatically* create a fiduciary relationship. Moreover, under pension legislation there is a clear distinction drawn between the role of an employer and the role of a plan administrator. This distinction was recognized by the Pension Commission of Ontario (“PCO”) in its decision in *Imperial Oil Limited v. Entitlement 55 Group* PCO Bulletin Vol. 6, Issue 4, p. 68. In that case, the PCO recognized that section 22 of the *Ontario Pension Benefits Act* (the statutory standard of care provision) did not apply to a company acting in its capacity as an employer when carried out functions of an employer such as creating, amending and winding up a pension plan, even if it was also the administrator of a pension plan. The PCO specifically acknowledged that an employer could amend a pension plan (i.e. deal with plan design issues) in its own interests.
- The Discussion Paper states at page 14 that Plan administrators of ECDCPPs are required to prepare a SIP&P. This is not true in all provinces. For example in Alberta, a SIP&P is not required if certain conditions have been met.
- The fictional scenario posed in the Discussion Paper to illustrate the issues faced by regulators, employers and administrators is not a realistic example and it may highlight issues that would never arise and may ignore issues that arise regularly. For example, the fictional example contemplates there is a large single employer ECDCPP administered by a board of trustees. This would be a most unusual situation since most such plans would be administered by the sponsor employer. The fictional scenario contemplates that the board of trustees actually manages the investment funds made available to plan members as investment options. We are not aware of any situation in which a board of trustees actually manages the investment funds that are made available to plan members.

IV. MISSING CONCEPTS

We discuss below various concepts that were not addressed in the Discussion Paper which we believe should have been dealt with in the Discussion Paper.

The Discussion Paper specifically excludes from its definition of CAPs, defined contribution pension plans in which the administrator is responsible for all investment decisions. The desirability for guidance to employers and plan administrators is, however, not confined to CAPs and there would be some value in providing parallel guidance where appropriate in relation to defined contribution pension plans in which the employer or the plan administrator makes all of the investment decisions. Accordingly, the Joint Forum should consider whether any of the principles it develops in relation to ECDCPPs should apply in cases where the plan administrator makes all investment decisions.

We recognize that administrators of CAPs must, in the administration of CAPs, comply with all applicable laws, including securities laws. However, the Disclosure Paper, in its discussion of the Securities Regulation regime seems to understate the responsibilities of the provider of the securities in the CAP context. In particular, the Disclosure Paper indicates that employers and plan administrators may have been relying on various securities exemptions in error and that it appears that “some plan administrators, employers and other third parties” do not comply with the requirements of the available securities exemptions and that therefore investment transactions involving some ECDCPPs are not in compliance with securities legislation.

With respect, the focus of the Discussion Paper on possible “non-compliance” with securities requirements by the employer or plan administrator reflects a misapprehension of the application of Securities Regulation which clearly regulates the sale or disposition of securities but not their purchase. It is the issuer of the security which bears responsibility for ensuring that there has been compliance with Securities Regulations. This makes sense because it is the issuer of the security and the promoter of the issuer who are compensated as a result of an investment made through a CAP. The employer receives no compensation and, indeed, usually covers much if not all of the administrative costs of making the CAP available to employees. Moreover, neither the employer nor the plan administrator are in the business of selling securities. The employer/plan administrator must rely on the assurances of the provider of the investment product that the sale by the provider of the investment product to the CAP complies with applicable Securities Regulation since that is intrinsic to the business of such provider.

If, as the Discussion Paper suggests, there is some doubt as to whether certain investment providers have had authority under Securities Regulation to sell certain products to CAPs, securities regulators have at their disposal all the powers they need to take action to restrain such investment providers and to ensure that purchasers of such securities are adequately protected. It would not make sense to impose additional obligations and costs on employers and plan administrators to ensure that the investment provider has complied with its obligations under Securities Regulation, especially after receiving assurance from the investment provider that it has so complied.

The Disclosure Paper does not seem to properly analyse the Insurance Regulation regime and how it applies to the majority of CAPs. For example, the Discussion Paper outlines the Insurance Regulation regime by focussing on the protections that regime offers to the insured. This discussion is somewhat misleading, since the discussion ignores the fact that a significant portion of moneys held in CAPs are invested in segregated funds of the insurance company which do not attract some of the protections described. For example, CompCorp does not protect moneys invested in segregated funds. Also, although there is a discussion of individual variable investment contracts (IVICs) and the protections provided to the investor, there is no evidence presented as to how many, if any, single person ECDCPPs are funded by way of an IVIC.

Also, in some CAPs either the employer or the plan administrator assumes responsibility for the investment of some contributions and the employee assumes responsibility for the investment of some contributions. The Discussion Paper does not outline how the proposed regulatory principles would apply in these type of CAPs.

CAP members bear the risk of investment loss associated with the contributions the employer makes and, if applicable, the contributions the CAP member makes. That is, if a CAP member proceeds to make imprudent decisions, after receiving or being offered the opportunity to receive full disclosure of all required information and other appropriate tools, that CAP member is responsible for the financial consequences of those imprudent investment decisions and not the employer or the plan administrator.

The fact that it is the CAP members who bear the risk of investment loss highlights the importance of members being provided with all the appropriate tools and other information required to assist them to make prudent investment decisions and of the role of CAP members.

However, one area notably absent from the Discussion Paper is any discussion of the responsibility of members of CAPs. Members who make investment decisions have a role to play - that is to become familiar with the information being provided to them, and to make prudent decisions. There should be an express recognition in regulatory policy and associated legislation/rules that the CAP member is ultimately responsible for his or her own investment decision and the financial consequences that flow from that investment decision, provided that the employer or administrator provides the member with all the information and appropriate tools required to make prudent investment decisions.

Related to the absence of any discussion of CAP member responsibilities is the absence of any meaningful discussion of the concept of providing employers and plan administrators a “safe harbour” from liability for the financial losses of plan participants as a result of their investment decisions. In fact, the Discussion Paper states at page 27 that, “[i]t is not proposed that plan administrators and employers would be held harmless for investment losses of members, if the principles were followed”.

With this statement, the Joint Forum rejects, without discussion or analysis, the possibility of making a “safe harbour” available to plan administrators and employers as part of the regulatory model for CAPs. At this stage while we do not express any view as to what the requirements should be for the grant of a “safe harbour”, we believe that the question of whether a “safe harbour” should be made available deserves greater consideration.

We therefore consider below whether making a "safe harbour" from liability for financial losses of plan participants available to plan administrators and employers should be part of the regulatory framework for CAPs. However, while we discuss the concept of providing a “safe harbour”, we do not consider in any detail what requirements a plan administrator or employer should satisfy to qualify for the “safe harbour”.

Before considering whether or not a “safe harbour” should be available to plan administrators and employers, it is important to understand what is meant by a “safe harbour”. In the CAP context, the concept of “safe harbour” comes from the *Employee Retirement Income Security Act* (“ERISA”) in the United States. Under s.404(c) of ERISA, if an administrator implements certain minimum design features in a member-directed, defined contribution pension plan, the administrator will have a defence or a “safe harbour” to member claims for financial loss as a result of their investment decisions.

The requirements that must be satisfied for an administrator of a member-directed, defined contribution pension plan to obtain the benefit and security of the “safe harbour” under s.404(c) of ERISA are quite detailed. In general, s.404(c) of ERISA provides a fiduciary in respect of a member-directed, defined contribution pension plan with a defence to member claims for investment loss if the plan provides members with an opportunity to exercise control over assets in their accounts and an opportunity to choose from a broad range of investment alternatives. The “safe harbour” requirements under ERISA include:

- the plan must offer at least three "core" investment options, each of which must be diversified and have materially different risk and return characteristics;
- plan participants must have control over the assets;
- plan participants must be able to reallocate assets at least on a quarterly basis; and
- plan participants must be provided with certain information to enable them to make informed investment decisions. The information which must be provided to plan participants automatically to obtain the protection of s.404(c) of ERISA includes:
 - (a) an explanation that the administrator may be relieved of liability for losses that are the result of the participant’s investment instructions;
 - (b) a description of the investment alternatives available under the plan, which includes a description of the investment objectives and risk and return characteristics;
 - (c) the identity of any designated investment managers; and
 - (d) a description of any transaction fees and expenses

The information which must be provided to plan participants upon request includes:

- (a) a description of the annual operating expenses of each designated investment alternative; and
- (b) copies of any prospectuses, financial statements and reports and any other materials relating to the investment alternatives that are provided to the plan.

Section 404(c) of ERISA works in an interesting manner. It operates by *encouraging* administrators of member-directed defined contribution pension plans to meet the requirements contained therein. Compliance with s.404(c) of ERISA is not mandatory. Rather, administrators of member-directed, defined contribution pension plans may *choose* to comply with s.404(c) of ERISA. Administrators of member-directed, defined contribution pension plans are encouraged or motivated to comply voluntarily with s.404(c) of ERISA because if they do, they obtain the benefit and security of an accepted defence to potential member claims for financial loss as a consequence of their investment decisions – the “safe harbour”.

The Discussion Paper has not discussed the possibility of making a “safe harbour” available to administrators and employers as part of the proposed regulatory principles for CAPs. Many of the proposed regulatory principles outlined in the Discussion Paper are in the nature of “best practices” and do not include a specific description of the regulators’ expectations. For example, some of the proposed principles use subjective terms such as “adequate”, “reasonable”, or “appropriate” when describing what is expected of the plan administrator/employer and do not include an explanation of what is meant by such terms.

If a “safe harbour” were to be made available, it would be necessary to clearly set out the regulator’s expectations of administrators and employers when providing investment choices to participants. This exercise would provide employers/administrators, participants, and regulators with certainty as to expectations and requirements.

Increasingly, the model for regulating industries and sectors involves “self-regulation”. Regulators simply do not have the resources to actively regulate each and every matter. Making a “safe harbour” available to employers and administrators would complement the self-regulatory model. If a “safe harbour” is available, administrators and employers will be encouraged to comply with the specified, minimum requirements required to obtain its protection and it would be considerably easier for the regulator to monitor compliance through its audit process.

We note that the experience in the U.S indicates that there are some practical issues relating to a “safe harbour” that will need to be addressed, including the following:

1. Some of the “safe harbour” requirements may be difficult to describe with clarity. However, this is no reason not to attempt to describe them.
2. Under ERISA there is a distinction between investment information and investment advice. Distinguishing information from advice can be a difficult distinction to make. The difficulty applies equally in the case of investment information versus investment advice. Guidance is required to assist in making this distinction.

Moreover, any “safe harbour” requirements that are developed should consider the interests of plan members and should reflect the principle that if a “safe harbour” is granted, the “safe harbour” requirements should be sufficiently clear and comprehensive to justify the grant of a “safe harbour”.

V. PROPOSED REGULATORY PRINCIPLE NO. 1 - OBLIGATIONS WITH RESPECT TO THE ESTABLISHMENT AND MAINTENANCE OF A CAP

Question - Appropriateness and Adequacy of the Regulatory Principles

- It is not clear that it is appropriate to capture all Group RRSPs, DPSPs and EPSPs under these proposals. For example, if non-pension CAPs are not intended to be retirement savings vehicles, then a different regulatory approach might be appropriate. Perhaps it would be better to indicate the structure a retirement savings vehicle must have to be caught by the rules. For example, a Group RRSP where there are no employer contributions and that permits employees to withdraw their money at any time might be inappropriate to capture under the proposed regime.

- It is appropriate for minimum standards to be identified, such that if the person responsible complies with these standards, there is a presumption (albeit a rebuttable presumption) that such person has complied with its obligations. The need for minimum standards to be specified to serve this purpose applies even if a “safe harbour” is not offered.

Question – Effective and Practical Methods of Implementation?

- It would seem that the most effective and practical method of implementing the proposed regulatory principles would be to amend the applicable pension, securities and insurance legislation in each province. In order to encourage harmonized rules to be adopted by the various jurisdictions, the Joint Forum should use the finalized principles to develop stand-alone model legislation/regulation for CAPs.
- A common set of best practices is to be encouraged, even over regional “improvement” in the rules.
- There is a strong need for a level playing field in the regulation of CAPS. Certain providers, such as insurance companies, should not be given a competitive advantage by virtue of being covered by different legislation.

Question – Anticipated Short-Term and Long term Costs

- There will be increased costs associated with additional regulation of this area. These increased costs will more than likely be passed on to the plan members either through increased investment management fees of providers or lower levels of company contributions. The effect on CAP members in both cases will be the same. The aggregate savings of CAP members will be diminished over the long term. However, imposing these additional costs on CAP members may be seen as appropriate if the regulator considers that without this additional regulation, CAP members will not receive the information and tools they need to make prudent and informed investment decisions and the long term costs of not having such information and the risk of making poor investment decisions as a result, outweighs the higher costs associated with complying with the additional regulation.
- Smaller employers may be discouraged from offering any savings vehicle at all.

The Discussion Paper suggests five duties which should be specifically included as part of the fiduciary duties of a plan administrator and/or an employer in the context of Proposed Regulatory Principle No. 1. In addition to our general comments above, we have the following specific comments on these specific suggestions.

1. Select investment options for members which offer a reasonable range of options with different risk and return characteristics, each of which is diversified.

- This could either be a plan design feature, which falls within the purview of the responsibility of an employer or the plan terms could be silent, leaving it to the plan administrator to deal with. Any regulatory principle that emerges in this regard should make it clear whether it applies only to plan administrators or whether it applies to plan administrators *and* employers.
- It is not clear how each option can be diversified. Does this mean that the only permissible investment option will be units of mutual or pooled funds or insurance company segregated funds which are themselves diversified? It would appear that a GIC option or the option to invest in shares of the employer or a related company would not be permissible under the above statement of principle. We assume that the Joint Forum merely intends that each investment option should be diversified from each other (option). If so, this should be expressly stated.
- Why cannot the regulator suggest the appropriate minimum standard? For example, the regulators could provide some indication of what is or is not a reasonable range. Is every available fund (i.e. the entire universe) a reasonable range? Is offering 3 funds with different risk and return characteristics a reasonable range? How different must the risk and return characteristics be? Should there be some minimum number required?

2. Prudently select, using all relevant knowledge and skill, the investment managers for each investment option.

- No comment.

3. Prudently monitor the performance of the investment managers for each investment option, including setting and monitoring benchmarks for investment performance according to the type of fund, and taking appropriate action where performance is unsatisfactory.

- It is not clear what is meant by “taking appropriate action”. Should it be up to the plan administrator or plan sponsor to terminate the appointment of the investment manager (or more likely, remove the particular fund as an available option)? If the plan administrator must take action what should be done with amounts already invested? Should CAP members be forced to liquidate these funds or should they be permitted to leave the money in the funds? Should the obligation be merely to advise the CAP member of the unsatisfactory performance?
- It would be helpful for minimum standards be set describing for example minimum frequency of such monitoring (eg. is annual monitoring sufficient?).

4. Where no prospectus is provided, ensure contracts with a third party provider or investment manager allow the plan administrator or employer to pursue an action on behalf of members for any misrepresentation about the investments.

- It is completely unrealistic to contemplate that an employer would be able to negotiate this as a term of a contract, unless the legislation clearly mandated that this be a term of all such contracts. The third party provider or investment manager will not agree to the inclusion of such a provision in their contracts with smaller employers and it is highly unlikely that they would do so for the largest employers. Moreover, who would pay the costs of any such proceeding? Is either the employer or plan administrator expected to fund any such legal proceeding? Who pays for the costs associated with the proceeding which cannot be recovered from the third party provider or investment manager? On what basis could the employer or plan administrator settle any such proceedings or even decide that costs of any such proceeding when compared with the chances of success in the proceeding did not warrant commencement of the proceeding. Would the employer or plan administrator be absolved from liability in these cases? This proposal is fraught with difficulties.
- This proposed requirement will lead employers towards using prospectuses. This will ultimately lead to increased costs to CAP members. Moreover, it is not clear that a prospectus will provide CAP members with any better disclosure than they get under the current system. The industry has been responding to the need for investment-related education for pension plans that offer investment choice for some time now, and there are some electronic programs, questionnaires and other tools that are available and could form the basis for a new disclosure regime.

5. Allow members reasonable opportunities to switch between investment options without penalty.

- It is not clear how this proposal should apply in relation to Guaranteed Term Investments (“GTI”) provided by insurance companies. With GTIs there is typically a penalty if the investor seeks to redeem the GTI prior to the expiry of the specified term. Is it intended that CAP members be able to, for example, lock-in to 5-year term rates in a GTI and then move out of such investment at no cost or penalty if interest rates go up, so that the plan member can reinvest in a GTI with a higher interest rate? This does not seem equitable.
- What is meant by “reasonable” must be defined more clearly. Some minimum guidelines as to what is a reasonable opportunity should be developed. Is once a month reasonable? Is once a quarter is reasonable? Is once every six months reasonable? There is no reason why a regulator cannot specify what the minimum standard should be.

VI. PROPOSED REGULATORY PRINCIPLE NO. 2 – OBLIGATIONS RELATING TO INITIAL AND CONTINUOUS DISCLOSURE

Question – Appropriateness and Adequacy of Regulatory Principles

We agree that both initial and ongoing disclosure of appropriate information to CAP members is a key regulatory principle.

The Disclosure Paper lists eight areas that should be covered in the initial disclosure. Our comments on each of those areas are as follows:

Area 1 - The Discussion Paper suggests that there be an explanation of the liability of the plan administrator or employer and of members for investments. We assume that this is intended to be a reference to disclosing that the member is responsible for investment decisions and gets the rewards from good investment decisions and conversely bears the risks of bad investment decisions. The Joint Forum's intent should be clarified.

Area 2 – The Discussion Paper refers to “instructions” on how to make investment choices. It is not clear whether this is intended to mean describing the administrative process for making investment choices or some more general discussion of the thought process a CAP member should go through when making investment decisions. If the latter is intended then this would create an obligation that was so vague in scope that it would be very difficult for plan administrator or employer to determine whether or not they had complied with the requirements. The intended scope of this requirement should be clarified.

Area 3 – No comment.

Area 4 – Disclosure should include *any* fees which CAP members bear not only management and investment fees. For example, if any “recordkeeping fees” are allocated to CAP member accounts, this should be disclosed.

Areas 5 and 6 – No comment.

Area 7 – It is not clear what is meant by a “standardized consumer guide”. What is meant by “standardized”? Will there be a requirement for a standardized format or only a requirement for certain standard information to be included? Who will be “standardizing” the contemplated consumer guide? Will it be the regulators? These points should be clarified.

Area 8 – No comment.

The Disclosure Paper also lists four areas that should be covered as part of continuous disclosure. Our comments on each of these areas is as follows:

Area 1 – It is not clear what is meant by “annual operating fees for each investment option”. This should be clarified.

Area 2 – It is not clear what is meant by “material change reports on changes to investment options”. This should be clarified.

Areas 2-3 – While it is possible that the plan administrator or employer may itself construct an investment option (e.g. an option to invest in shares of the employer or a related company) in most cases the investment options offered will be investment products offered by third parties. In these situations neither the plan administrator nor the employer will have the information necessary to generate things such as “material change reports”, “financial statements for each investment option” or “asset lists of the portfolio for each investment option”. Indeed, where CAP moneys are invested in insurance company segregated accounts which holds units of a pooled fund operated by an investment manager, even the insurance company may not be in a position to provide such information. It is the investment manager or third party provider of the investment product that is better equipped to produce these reports, statements and lists. The responsibility of the plan administrator or the employer should be confined to ensuring that CAP members have access to information of this kind provided to them by the investment managers.

Area 4 – No comment.

Question – Effective and Practical Methods of Implementation

As indicated above, the plan administrator or employer may not have access to the information which the Joint Forum contemplates will be provided to CAP members. While the ultimate investment managers may be prepared to provide that information to the plan administrator, this is not something that should be left to chance and/or the ability of the plan administrator or employer to negotiate in its contract with the provider of the investment product.

If the regulators intend to impose on the plan administrator the obligation to provide this kind of information, legislation will be necessary to ensure that the ultimate investment managers who have this information have a legal obligation to provide such information to the plan administrator or employer.

Question – Anticipated Short-Term and Long-Term Costs

There are two main components to the costs associated with making initial disclosure and ongoing disclosure with the level of detail contemplated. One component relates to the cost of gathering the information and putting it together in a readable and comprehensible form and format. The costs of so doing will typically be passed on the CAP member either explicitly or implicitly through higher fees charged by the investment manager. The second component relates to the cost of actually printing the information and distributing the information to CAP members. The Joint Forum should clarify the media through which such information could be provided (e.g. would providing the information in electronic format be sufficient?) and whether or not this is information that must be provided to every CAP member or if it would be sufficient to provide it to members on request.

VII. PROPOSED REGULATORY PRINCIPLE NO. 3 – RELIANCE ON ADVICE OR INVESTMENT INFORMATION FROM A FIDUCIARY

Question - Appropriateness and Adequacy of the Regulatory Principle

The Joint Forum proposes that the plan administrator or employer fiduciary duties should include the duty to ensure that members deal with a registered sales representative or advisor (the “Advisor”). Any specific proposals that come out of this regulatory principle should make it clear whether the obligation or duty that is to be imposed is an obligation or duty of the plan administrator or the employer.

The Joint Forum’s suggestion has a heavy “securities” flavour and focus. There is a reference to reviewing member’s investment choices for suitability based on their “Know Your Client” profile. We note that the securities regulators have recognized that it is not necessary to apply the “Know Your Client” rule in all cases, as they have eliminated this rule for so called “discount brokers”. The Disclosure Paper does not address whether this has any impact on the rationale for the suggestion that the plan administrator or employer should review member’s investment choices for suitability based on their “Know Your Client” profile.

Moreover, the way the proposed duty is formed leaves more questions than answers. For example:

- How does one “ensure” that the CAP member deals with a registered sales representative or advisor?
- Must the CAP be provided on the basis that plan members cannot make investments without so dealing?
- Some employees may not want to use the Advisor's services, on the belief that they are savvy enough to make their own investments but the proposed duty appears to have the effect of forcing the employees to do so. What happens to members’ contributions and the employer’s contributions if the CAP member does not speak to a registered sales representative or advisor?
- Would it be sufficient to recommend to the CAP member that he or she seek out a registered sales representative or advisor?
- What methods should be used in choosing a sales representative or advisor and what would constitute reasonableness in making such a choice?
- How far must the employer or plan administrator go in ensuring that the Advisor carries out his duties in an appropriate manner?
- Is the employer or plan administrator entirely relieved of all responsibility and liability if the employer or plan administrator selects and monitors an Advisor in a "prudent" manner? In other words, at what point can the employer or plan administrator stop worrying about potential risks?

- Must the employer or plan administrator request regular reports on whether employees are using the Advisor's services?
- Who is liable if the advice given by the Advisor is bad or insufficient?

Further, it is not clear who is to pay for the Advisor's services. Investment and financial planning advice can be costly. If the employee is to pay, he may want input as to whether he wishes to use an Advisor selected by the plan administrator or employer or one of his own choosing. **The effect of requiring that a member deal with an Advisor may be to ask that a significant portion of either the contributions to the CAP or a significant portion of the gross investment return on the contributions in the CAP member's "account" be utilized for investment advice.**

The Discussion Paper proposes that, as an alternative to dealing with an Advisor, the plan administrator or employer may take reasonable steps to ensure that the members receive initial and continuous investment information and receive appropriate assistance in making investment decisions. These steps can include a review of member's investment choices for suitability or creating a process to allow members to communicate investment information needs to the plan administrator or employer.

This alternative proposal is fraught with difficulties. The use of surveys and reviewing member's investment choices raises some concern with respect to privacy issues. The use of surveys and requesting information about member's investment choices is too intrusive. CAP members will be rightly concerned about giving extensive personal financial information to the employer or plan administrator. For instance, a plan member may have very conservative investment choices based on other factors such as a spouse being a member of another pension plan, or expectation of an inheritance. These are not factors that a member should have to reveal to the plan administrator or employer in "justifying" his or her investment decisions.

Further, the plan administrator or employer (not being in the business of providing investment advice) would not be in a position to advise whether particular investment choices are appropriate. In practical terms employers and plan administrators would not subject themselves to these difficulties and the Advisor's route with its "securities" focus would be the only one adopted with its associated costs.

Question – Anticipated Short-Term and Long-Term Costs

For an employer the cost of providing investment advice will include both time and money. There will be time spent in selecting an appropriate Advisor and monitoring the Advisor to ensure risks are reduced. The dollar cost is not easily quantified, but providing investment and financial planning advice can be expensive, regardless of whether the employer or plan member pays for it. A cost/benefit analysis of providing a savings program may indicate that it would be easier for an employer to increase salaries allowing employees to invest on their own outside of a DC retirement savings vehicle. This is especially true for smaller employers. The avoidance of unnecessary costs that discourage the growth and use of CAPs must be considered.

The anticipated costs should, however, also be considered in light of the costs to employees if they do not receive appropriate investment advice. Employees who do not receive appropriate investment advice will not have all the tools that they require to make informed investment decisions and as such may experience investment losses. Further, the anticipated costs should also be considered in light of potential costs to employers if they do not provide a salary and benefit package that is attractive to employees.

VIII. PROPOSED REGULATORY PRINCIPLE NO. 4 – THE INVESTMENT PRODUCTS OR FUNDS MUST COMPLY WITH MINIMUM STANDARDS

Question - Appropriateness and Adequacy of the Regulatory Principle

The Discussion Paper indicates that “[E]ach investment option should comply with minimum investment rules designed for CAP investment options, to ensure, among other things, adequate diversification of funds, the avoidance of conflicts of interest and an acceptable level of risk.” The proposed content of these rules and our response is noted below:

1. Avoidance of conflicts of interest.

It is not clear what conflicts of interest the Joint Forum is concerned about in relation to CAPs. Plan sponsors derive no financial gain from CAPs, other than the acquisition and retention of their employees, and their obvious concerns regarding their employees’ well being. Conflicts of interest that should be avoided should be specified. For example, is there a conflict of interest if an employer offers as an investment option, shares in the employer or a related company? Is there a conflict of interest if one of the investment options is a fund which holds shares of the employer or a company related to the employer?

In the securities industry there are obvious conflicts of interest. For example, conflicts of interest in the securities area, because compensation of advisors is based in part on the volume of activity in an account and because the promoter of the securities receives compensation based on the volume of securities sold. This is not a factor in CAPs. Simply stated, the securities industry is driven by a profit motive, which requires adequate supervision and rules to avoid actual and perceived conflicts of interest. The focus on conflicts of interest as an area that needs to be addressed, is an example of a focus on “securities” regulation issues which do not arise in relation to CAPs.

2. CAP members be able to withdraw their retirement funds at any time, or change their asset allocation into other investment options.

It is not clear what is intended by the recommendation that a member be permitted to withdraw retirement funds “at any time”. Funds in defined contribution pension plans are subject to locking-in provisions associated with legislation governing pension funds. Is it intended to override the locking-in rules? Most, if not all, provinces take the position that Plan members cannot exercise a portability option prior to termination of employment. Is it intended to override this requirement and let CAP members withdraw funds from registered pension plans at any time? If not, what is intended?

The suggested model seems more in keeping with retail security investments rather than pension funds.

3. Since CAPs are intended as long term savings vehicles aimed at retirement, the available investment options be limited to avoid excessive risks.

As indicated in our previous comments, we do not agree that all CAPs are intended as long-term savings vehicles aimed at retirement. It follows that any “investment rules” should reflect that the use of the CAP by CAP members may need to serve many different purposes. Some CAP members may wish to invest these funds in risk-oriented investments because the administrative costs associated with group plans is less than the costs and fees associated with so-called “retail” investments. Others may wish to invest their funds in the publicly-traded shares of their employer, if available, if they believe that is their best investment choice. Under this principle, would this involve an “excessive risk”?

Also, it is not clear what is meant by “excessive risks”. CAP members reflect a diverse group. The level of education, skill sets, as well as investor knowledge/sophistication does not easily lend itself to setting investment rules specifying what are “excessive risks”. This concept is so vague as to be meaningless. If the Joint Forum is of the view that certain types of investments should not be made available under CAPs then those investment should be specified with some clarity.

4. CAP members should not be subject to greater risks than investors in retail mutual funds or segregated funds.

It is not clear what is intended here. Who would be required to judge the relative risks that investors might face in a retail mutual fund or a segregated fund? Is the employer or plan administrator required to compare the relative merits of an investment option offered through a retail mutual fund or a segregated mutual fund? How are GTIs to be considered in this context?

Question - Effective And Practical Methods Of Implementation

The investment rules that are adopted must not be so onerous that employers will no longer provide CAPs as part of their total compensation package. Any investment rules proposed should both protect members and facilitate the growth of employer-sponsored CAPs.

Therefore, if investment rules are required to define the acceptable level of risk, the rules should also define who bears the risk. In making their investment decisions, CAP members have to bear some responsibility for the choices they make. It would be inappropriate to expect an employer or plan administrator to assume the entire risk associated with the adequacy of an individual’s investment choice(s).

Furthermore, if the entire burden is borne by the employer/plan sponsor, then in order to avoid future liability, it might be essential to understand the CAP member’s entire financial history. This would obviously lead to privacy issues and legislation may be required in order to override protections that might otherwise be provided by applicable privacy legislation.

Question – Anticipated Short-term and Long-term Costs

It is obvious that the more onerous the investment provisions, the more likely it is that employers will no longer be encouraged to use CAPs as a part of an employee's total compensation package. In the short-term, employers/plan sponsors will likely remain on the "sidelines" and use alternative methods of compensation for their employees until the impact of CAP regulation is clearly understood. At this point, the long-term impact of investment rules on the use of CAPs is too speculative to consider. However, the risk of increased future liability to employers/plan sponsors certainly is not encouraging.

In terms of the dollar costs associated with the creation of investment rules, there are other factors to consider. If we are to examine the ultimate advantage of CAPs from an investment perspective, then it is clear that a major advantage of employer-sponsored CAP plans is the lower fee schedule as compared to a similar "retail" investment.

The anticipated costs should, however, also be considered in light of the costs to employees if they do not receive appropriate investment advice. Employees who do not receive appropriate investment advice will not have all the tools that they require to make informed investment decisions and as such may experience investment losses. Further, the anticipated costs should also be considered in light of potential costs to employers if they do not provide a salary and benefit package that is attractive to employees.