# Delivering on the Target Benefit Plan

## Third in a series of Guides on Target Benefit Pension Plans published by Aon Hewitt

### Governance and Risk Alignment

The target benefit pension plan continues to gather momentum within the pension industry in Canada. Pension professionals, government officials, plan sponsors and employee groups are actively examining how these plans could work. Legislation is being drafted across the country. There is growing support for the notion that the target benefit approach can play a key role in delivering more sustainable pension plans in the future.

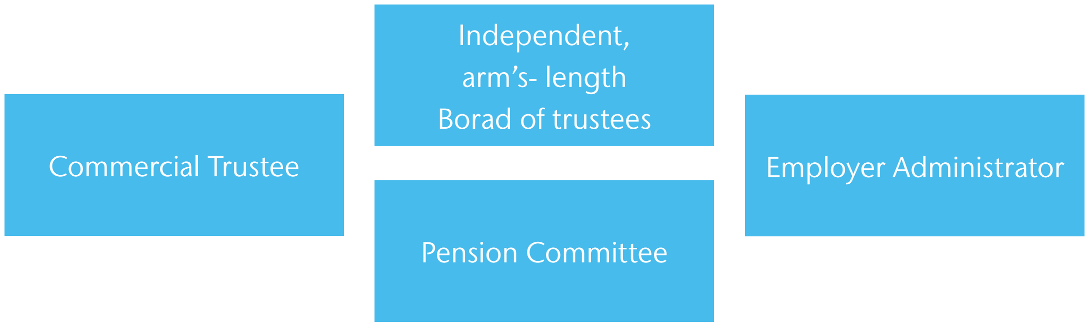
In this, the third in a series of guides on target benefit pension plans published by Aon Hewitt, the attention turns to governance of these fixed contribution, variable benefit pension designs, taking a close look at key considerations, possible governance alternatives, and options for pension regulators.

"Plan design and pension governance need to be aligned," says Roy Stuart, Associate Partner, Retirement with Aon Hewitt, and one of the guide's authors. "By this, we mean that the pension governance structure should provide the parties who are exposed to risk with the power to manage their risks."

In a target benefit plan, members clearly have the greatest exposure to financial risk – the risk of not receiving the benefits at the targeted level. Nevertheless, employers involved with setting up a target benefit plan have significant reputational risk and talent risk. From both a human resources perspective and a financial perspective, the employer will not want the plan to appear to have failed and will therefore have a large stake in its success.

*Governance and Risk Alignment* presents several considerations that impact the governance of a target benefit plan. Whether the arrangement is collectively bargained (the typical situation thus far) or not will clearly impact the governance structure. The need to align governance with the unique risk sharing arrangement inherent in target benefit plan design suggests that a substantial measure of governance control be transferred from the employer. The New Brunswick legislation provides one possible answer: that the governance structure require an independent plan administrator.

The composition, role and competencies of an independent plan administrator are examined carefully. The guide further proposes a spectrum of alternatives for the administrator:




The choice of administrator would be influenced by the plan's stakeholders views on balancing security, transparency, and control:

- The Commercial Trustee model involves contracting the work to a trust company, an option which could be expected to provide a high degree of security;
- The Pension Committee option contemplates a committee with member representation that is assigned the powers of administrator, as already provided for in Manitoba and Quebec pension legislation. A well-functioning Board of Trustees or Pension Committee, with member representation, provides the most opportunity for transparency to members. One of the most vital aspects of the target benefit concept is that members understand the true nature and extent of the plan's promises.
- An employer management team would give the employer the most control.

Some might be concerned about the concept of the employer as administrator. While there are certainly reasons an employer might not want the role of administrator, the guide challenges the thinking that the employer cannot be the administrator by making two observations:

1. There are no such concerns in respect of the typical DC pension plan, where the employer is often the administrator, even though employees bear more risk than with a target benefit plan;
2. By setting up a target benefit plan, the employer takes on the role of helping individual employees manage their pension risks. This is perhaps a paternalistic view, but it is also one of the reasons for considering target benefit instead of DC.

From a regulatory point of view, the guide anticipates that policymakers will want to protect members by implementing a fairly strict regulatory burden regarding benefit/funding policies and ongoing sustainability testing, but that this might then allow more flexibility with governance. One key question raised is the extent to which plan members are bound by decisions made by pension committee members, particularly where there is no union and no vote. Pension legislation that clarified this would strengthen the hands of non-union and retiree representatives.

Target benefit plans can cover all types of members. The governance solutions may not be immediately obvious, but they are not impossible either. The Ontario Arthurs Report suggested that the presence of plan member appointees on the governance body is one of the strongest governance safeguards possible. Because of the allocation of risk between employer(s), employees, and, potentially, pensioners, member involvement in the administrator's function is critical to the long-term success of target benefit plans.

There is also a role for the administrator to play in providing professional assistance to members to manage their risks. The governance of a target benefit plan requires a distinction between the administrator and the stakeholders, with clear responsibilities and powers for each. With rigorous legislation concerning governance and risk management expectations, perhaps we can be considerably less concerned about exactly who must be involved in the governance of such plans.

To request a full copy of the guide, and for more information email info@aonhewitt.com.

## We're here to empower results

To learn more about how we can create custom solutions for your organization, please contact us:

Calgary, AB
+1.403.267.7010

Edmonton, AB
+1.780.423.1010

Halifax, NS
+1.902.429.7310

London, ON
+1.519.434.2114

Montreal, QC
+1.514.982.4806

Ottawa, ON
+1.613.728.5000

Quebec City, QC
+1.418.650.1119

Regina, SK
+1.306.569.6749

Saskatoon, SK
+1.306.934.8680

Toronto, ON
+1.416.868.5500
+1.416.225.5001

Vancouver, BC
+1.604.683.7311

Winnipeg, MB
+1.204.954.5500



June 2015