Going Forward: Plan design

What is QDIA and why have it?

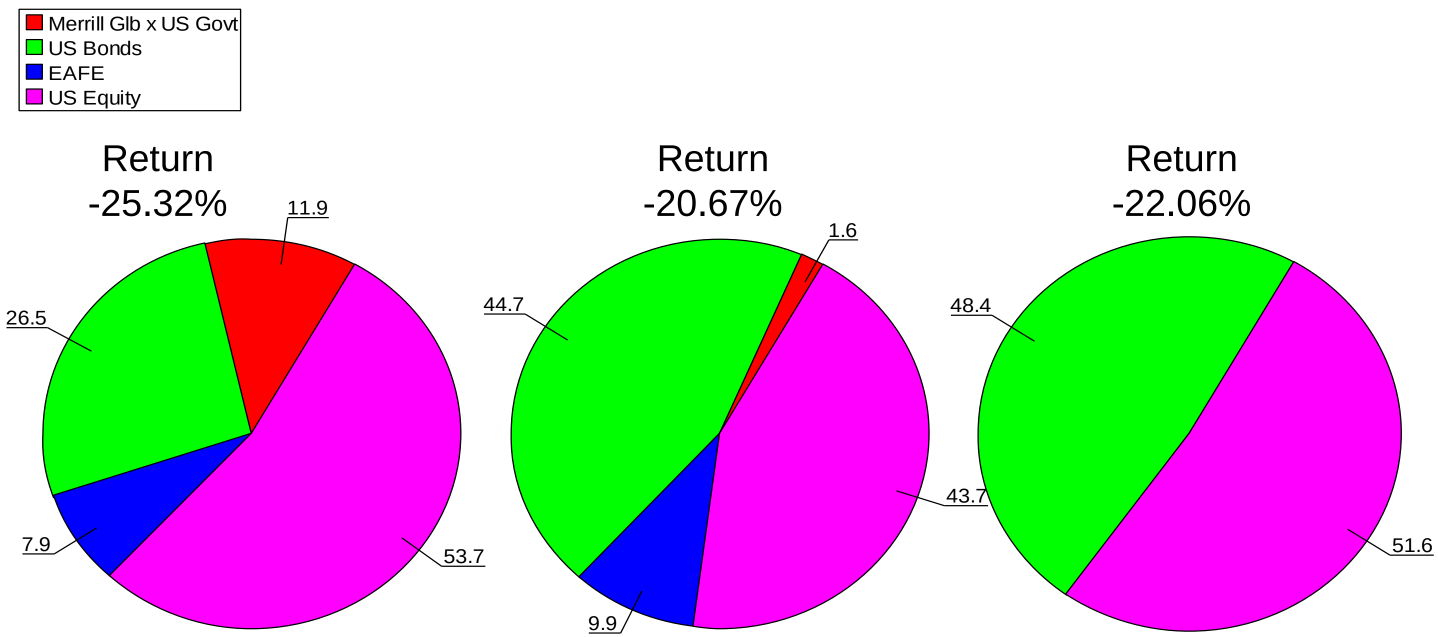
- Safe harbor default investment that offers ERISA 404(c) protection to fiduciaries for investment performance
- Types of Investments
  - Diversified so as to minimize the risk of large losses"
  - Must include a mix of equity and fixed income investments
  - Limited use of employer securities as QDIA investments
  - One of the following: target fund (to age, retirement date or life expectancy), balanced fund ("appropriate to participants as a whole") or investment management service
- No financial penalties and participants must be able to transfer balances out of QDIA at least quarterly
- QDIAs are default investments only; participants must be allowed to elect other investments
- Initial and annual notices and investment materials describing QDIA

Going Forward: Plan design

- Target–date funds
  - What is fund's objective?
    - Accumulation (risk-based)
    - Distribution (liability-based)
  - Reconsider volatility
- Alternatives
  - Balanced fund
  - Investment management service
  - Global tactical asset allocation fund

Asset Allocation

Total Return - January 08- December 08



Fidelity Freedom 2010

Vanguard Target Retirement 2010

60% S&P 500/40% BC Aggregate

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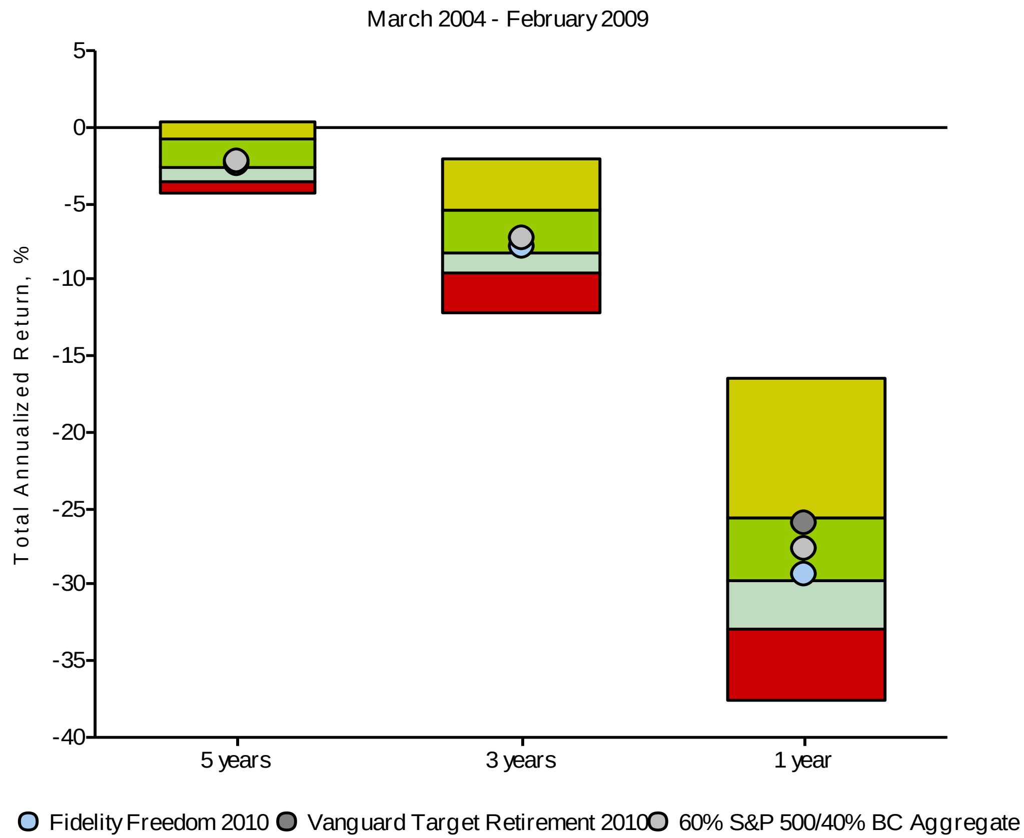
Annualized Returns

Fund	5 Years	3 Years	1 Year
Fidelity Freedom 2010	-2.44%	-7.94%	-29.41%
Vanguard Target Retirement 2010	NA*	NA*	-26.07%
60% S&P 500/40% Aggregate	-2.66%	-7.24%	-27.65%

*Fund is not old enough for this data point



Going Forward: new assets in the mix?

- TIPs
- Commodities
- Who mixes?
- Partial 404(c) plan?
  - Participant direction of own contributions
  - Professionally-managed fund for employer contributions
  - Professionally-managed fund could be QDIA, too

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Comparing Financial and Fiduciary Risks DB v DC Plans – The Canadian Landscape

- In DB Plans, the *Pension Benefits Act* (provincial/federal) governs
- In DC Plans, the PBA governs too, but few DC rules
- *Guidelines for Capital Accumulation Plans* published in May, 2004 by the Joint Forum of Financial Market Regulators
- Covers registered DC Plans and group RRSPs (401K-style)
- Purpose of Guidelines is to circumscribe the rights and responsibilities of CAP sponsors, service providers and members
- Are there voluntary guidelines or quasi-legislative standards?
- Lack of legislative standards presents a number of risks in converting from a DB plan to a DC plan. While employees increase their overall investment risks in DC, employers replace their DB investment risk with a new set of DC legal risks.

RISK #1 – NO SAFE HARBOR

- In the U.S., the pension legislation, ERISA, contains statutory safe harbors to insulate an employer from liability if all the prescribed steps are properly taken.
- In Canada, the CAP Guidelines are quasi-legislative and set out best practices for employer, however there are no safe harbors to protect employers.
- DC plans are in their infancy – few standards – despite that there are now more DC plans (8000) than DB plans (7000)

RISK #2 – DC CONVERSIONS

- Contribution holiday risks – Employers who want to convert from DB to DC to take DC contribution holidays from the DB pension trust surplus *Nolan v. Kerry (Canada) Inc.* (2009 SCC)

- Salary scale risk – *Halliburton* case (2010 Alta CA) – An amendment freezing salary at conversion date for employee could be a "void" amendment under PBA legislation

RISK #3 – PLAN DESIGN RISK

- Section 2.2 of the CAP Guidelines puts the responsibility on the employer to design the plan's investment options.
  - *"The CAP sponsor should ensure a range of investment options is made available taking into consideration the purpose of the CAP".*
- There may be a duty of care or fiduciary duty owed to the plan members associated with the range and design of the plan's investment options.
- Giving employees an "inappropriate" or "undiversified" choice of funds could give rise to liability and damages if the funds' performance are inadequate.

RISK #4 – COMMUNICATION RISK

- In DB Plans, there is little ongoing communication between the plan administrator and the plan members
  - E.g., Annual statements, termination statements, portability options, joint and survivor options, certain plan amendments.
- In DC Plans, there is regular and ongoing communications between the parties:
  - CAP s. 3: Investment decision making tools for members
  - CAP s. 4: Investment and transfer options
  - CAP s. 5: Ongoing Communications

RISK #5 – DELEGATION RISK

- Duty to supervise agents of the plan administrator: PBA s. 22(7).
- In a DB Plan, the typical agents include the H.R. department, the actuary, the investment manager, the custodian, the lawyer.
- A DC plan has more service providers:
  - **CAP Guidelines S.1.3.1** – Employer may delegate responsibilities to a "service provider"
  - **CAP Guidelines: Section 3.4** – Employer may *"provide the members with <u>advice about their investment decisions</u>"*
- DC Plan service providers will be directly communicating with and possibly giving advice to Plan members.
- More misunderstandings.