Pensions

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Executive summary

Pension plans are complicated arrangements. They need appropriate management and oversight to fulfil the pension promise. The Government's pension plans need sound governance practices in the oversight and management of the plans.

If governance practices are not adequate, the Government may have difficulty paying the pensions promised. Also, the pension plans may not have sufficient assets to provide reasonable pensions to members. Good governance practices help to ensure that the Government can pay the pensions promised and that the plans can provide reasonable pensions.

In this chapter, we outline the criteria that we will use to audit the governance practices used by the Government's pension plans. Pension plans should have rules and procedures to ensure that:

- Board members have adequate knowledge. We expect pension plan boards and management to have a clear understanding of what they do, why they do it, and to whom they are accountable.
- The board approves an appropriate delegation of authority. We expect tasks to be properly delegated and authorized in accordance with the requirements of legislation and plan arrangements.
- Board decisions are properly documented. We expect pension plan boards to have clearly set out their role and responsibilities in writing.
- The board monitors operations on an on-going basis. We expect the pension governance practices to include timely reporting by management to the pension plan board.
- The board has an appropriate external communication policy. We expect the pension plan board to approve a written external communication policy.

Over the next few years, we plan to audit and report on the governance practices used by the Government's pension plans using the criteria outlined in this chapter.

Glossary

Defined benefit pension plan – a pension plan that specifies the pension that members of the plan receive on retirement or the method of determining the pension.

Defined contribution pension plan – a pension plan in which the members' contributions are fixed, usually as a percentage of pay (except for the Saskatchewan Pension Plan, whose members can contribute up to $600 each per year). A member's pension is based on the member's and the employer's contributions made on behalf of the member and investment earnings on those contributions.

Fiduciary responsibility – under common law, board members owe a duty of loyalty to those persons whose interests they are protecting. Board members cannot be in a conflict of interest with their board duties or profit from their board duties because of personal interests. Board members must deal fairly with the members of the plan.

Government enterprises – are Government organizations that have the financial and operating authority to carry on a business. This includes contracting in their own name and selling goods and services to individuals and non-government organizations as their principle activity and source of revenue (e.g., Saskatchewan Power Corporation, SaskEnergy Incorporated).

Government service organizations – are those organizations that are accountable to the Government, either owned or controlled by the Government, and are not Government enterprises (e.g., Saskatchewan Health, Saskatchewan Education).

Pension liability – the present value of pension benefits earned as determined by an actuary using the pension plan's best estimates about future events and an appropriate actuarial method as recommended by The Canadian Institute of Chartered Accountants for accounting purposes.

Pension plan board – is the oversight body identified in the pension plan's act or plan document that acts as the administrator and is the body to which plan management reports. The pension plan board may be referred to as a committee, commission, or trustees in some cases.

Unfunded liability – the amount by which the pension liability exceeds the assets of the pension plan.

Purpose of chapter

When a pension promise is made, this is the first step in the creation of a complex arrangement known as a pension. The appropriate management and oversight of this complex arrangement is critical to the fulfilment of the pension promise for both defined contribution and defined benefit plans. The Government's pension plans are no exception. In this chapter, we outline the criteria that we will use to audit the governance practices used by the Government's pension plans.

If governance practices are not adequate, the Government may have difficulty paying the pensions promised for its defined benefit pension plans. For Government run defined contribution pension plans, the Government and its members may find that there is not adequate money in each member's account to provide a reasonable pension. Good governance practices help to ensure that the Government can pay the pensions promised.

In Saskatchewan, most Government pension plans have their own Acts. A few, under *The Pension Benefits Act, 1992*, have plan documents. The Acts and plan documents are complicated. Also, each Act or plan document is unique. These Acts or plan documents give varying powers and duties to the pension plans' oversight bodies (the pension plan boards).

These complexities and differences from plan to plan increase the risk that the plan, the board, or the Government may inadvertently make a mistake, or be perceived to have made a mistake. If a mistake occurs, the members of the plan, collectively or individually, can hold the parties involved accountable.

The problems that can occur are not restricted to a direct violation of a specific section of a pension Act or plan document, but can involve the application of common law. In recent years, the courts have increasingly used the concept of fiduciary responsibility as a tool to remedy perceived inequities. The Supreme Court of Canada has dealt with the issue of fiduciary obligations in a number of recent cases. While the concept of fiduciary duty is complex and subject to different interpretations, the one overriding feature of a fiduciary relationship is the dependency or vulnerability of the beneficiary.

The dependency or vulnerability of the beneficiary can range from the use of surpluses, to day-to-day decisions, and in some cases, to the right to receive a pension. In several Government pension plan Acts, wording, such as, “no allowance shall be granted to the widow or child of a superannuate or employee if the widow or child is in the opinion of the board unworthy of it”, still exists. Obviously, pension plan boards have the ability to exercise significant power over beneficiaries.

In the use of this power, there is risk that the board may not fulfil its fiduciary responsibility in a given case or cases and/or across a period of time. Good pension governance practices can manage and control this risk. The Government can reduce the risk of lawsuits by ensuring that boards of pension plans use sound governance practices.

The Government's pension plans are significant to the Legislative Assembly, members of the pension plans, and the public. Through the plans, the Government manages a significant amount of assets and pension liabilities. Note 6 to the Government's summary financial statements for the year ended March 31, 2001 shows an unfunded pension liability of $3.9 billion for government service organizations and a pension surplus of $241 million for government enterprises.

For the last several years, we have examined and reported on the systems and practices pension plans use to manage their key risks. Over the next few years, we plan to examine governance practices for the Government’s pension plans.

Our planned audit objective

The objective of our audit is to assess whether the Government’s pension plans have adequate governance practices.

Criteria

Auditors use criteria to evaluate the matters that they examine. Criteria are reasonable and attainable standards of performance and control against which auditors can assess the adequacy of systems and practices. We developed criteria based upon our review of international literature. We discussed the criteria with the Government’s pension plans. They agreed with our criteria.

We will use the following criteria to assess the adequacy of the governance practices of the Government's pension plans.

Pension plans should have rules and procedures to ensure that:

- Board members have adequate knowledge.

  We expect pension plan boards and management to have a clear understanding of what they do, why they do it, and to whom they are accountable. Boards need to carefully articulate and define a clear mission statement for their plans. Boards and management need to be qualified and knowledgeable to adequately perform their duties and tasks. To maintain qualified and knowledgeable board members and management, we expect pension plans to have a written succession plan that identifies the required skills and knowledge base.

- The board approves an appropriate delegation of authority.

  We expect tasks, that are delegated either to outside professionals (e.g. actuaries, custodians, investment managers, asset consultants, etc) or internally, are properly delegated and authorized in accordance with the requirements of legislation and plan arrangements.

- Board decisions are properly documented.

  We expect pension plan boards to have clearly set out their role and responsibilities in writing. We also expect that the decisions regarding the investment of the money in the pension fund and the selection of agents will also be in writing. We expect this written evidence of decisions to include all relevant information including the management of key risks. Management should prepare and the board should approve a strategic plan that includes a summary of the risks faced by the plan and its members, the key strategies to manage those risks, and the goals and objectives of the plan.

- The board monitors operations on an on-going basis.

  We expect the pension governance practices to include timely reporting by management to the pension plan board. The information provided to the board should include sufficient detail so that board members can understand and challenge management and/or outside professionals. Management should ensure that their reports and the reports of outside professionals are timely, accurate, and complete. To assist the board and employees in making decisions, we expect that the boards will have a written code of conduct for board members, management, and employees of the plan. We also expect a formal process of governance self-assessment. This includes reviewing and modifying the governance process over time to ensure its continuing effectiveness and reporting assessments to the appropriate stakeholders.

- The board has an appropriate external communication policy.

  We expect the pension plan board to approve a written external communication policy. The communication policy should ensure that disclosure is appropriate and timely. The board must have processes to ensure that the annual report distribution is to the appropriate stakeholders (those that own and/or share risk). The annual report should disclose the plan's governance principles and practices, and whether the board and management followed the practices. Where there has been a violation of the governance principles and practices, we expect that the report will provide an explanation. We expect plan members to be fully informed and educated when they bear the investment risk.

Our plan for the next few years

We plan to continue to examine the systems and practices pension plans use to manage their key risks. Specifically, over the next few years, we plan to audit the governance practices used by the Government's pension plans using the criteria outlined in this chapter.

In addition, in a future report, we will provide an update on the progress of our past recommendations and the progress that pension plans have made in improving their annual reports.

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