Chapter 3
Section
3.03

Financial Services Commission of Ontario—Pension Plan and Financial Service Regulatory Oversight

Background

The Financial Services Commission of Ontario (FSCO) is an agency accountable to the Ministry of Finance and responsible in Ontario for regulating pension plans; the insurance industry; the mortgage brokerage industry; credit unions and caisses populaires; loan and trust companies; and co-operative corporations. Credit unions and caisses populaires differ from banks in that they are owned by their members and are generally non-profit organizations. Co-operative corporations (known as co-ops) are owned and controlled by their members and pool their resources to provide members with products, services, workers and housing.

FSCO's mandate is to provide regulatory services that protect the public interest and enhance public confidence in Ontario's regulated financial sectors through registration, licensing, monitoring and enforcement. FSCO also makes recommendations to the Minister of Finance on legislation and regulations relating to regulated financial sectors. FSCO's senior official, the Superintendent of Financial Services, is responsible for the general supervision of pensions and the regulated financial sectors under the *Financial Services Commission of Ontario Act, 1997* and 11 other statutes that govern the regulated sectors.

Financial institutions are subject to both market-conduct regulation and prudential regulation.

Market-conduct regulation focuses on the relationships between consumers and licensed or registered businesses and individuals, and between pension plan members and pension plan administrators. Market conduct, or the conduct of business, is influenced by many factors, including the legal framework, established best practices, codes of conduct and the expectations of consumers or pension plan members.

Prudential regulation focuses on financial stability and the long-term ability to meet financial obligations. This type of oversight applies to financial institutions such as insurance companies, credit unions or caisses populaires, and pension plan administrators.

In the 2013/14 fiscal year, total FSCO operating expenditures were $87.9 million, of which about $29 million was spent by its Pension Division and Licensing and Market Conduct Division. The remaining expenditures related to regulation and oversight of the auto insurance sector, the subject of an audit we conducted in 2011. FSCO employs about 150 staff who deal directly with pension plans and the regulated financial sectors, and it recovers 98% of its costs in these areas from regulated bodies.

Pensions

The Pension Division of FSCO is responsible for the administration and enforcement of the *Pension Benefits Act* (Act) and supporting regulations. The Act requires every employer that establishes a pension plan in Ontario to register the plan with FSCO and comply with the reporting and fiduciary responsibilities set out in the Act. Pension plans are administered by a plan administrator, who may also be the employer sponsor. The Act covers employees who currently work, or previously worked, in Ontario (and in some cases other jurisdictions) and who are members, former members with a deferred pension or retired members of a provincially regulated pension plan. Pension plans in federally regulated industries such as banking, telecommunications and airlines are overseen by the federal Office of the Superintendent of Financial Institutions.

The pension benefits paid to members depend on whether the plan is a defined-benefit plan, defined-contribution plan, or a hybrid of the two.

In a defined-benefit pension plan, the amount of pension income a member will receive each year after retirement is predetermined, and calculated using a defined formula usually based on years of employment, age at retirement and salary level, or a flat dollar amount. While employers and employees (in contributory plans) contribute to the plan, employers typically assume the financial risk that there may not be enough money in the plan to pay for future benefits because of volatility due to fluctuating investment returns and interest rates.

A defined-contribution pension plan, on the other hand, is less risky for employers because the level of future annual pension payments is not predetermined. Instead, it is based solely on the sum of employer and employee contributions over time and investment returns on those contributions, minus administration costs. Members do not know how much their pension benefits will be until they retire, and the plan administrator has no obligation to pay out more than the funds available in the plan.

Figure 1 describes the more than 7,300 pension plans, with about 3.8 million members, registered with FSCO. As of August 31, 2014, FSCO regulated 3,487 defined-benefit plans, 3,150 defined-contribution plans and 686 hybrid plans. For purposes of reporting, FSCO treats all hybrid plans as defined-benefit plans. The **Appendix** provides a three-year summary of pension plans by type and membership.

The Pension Benefits Guarantee Fund (PBGF) was established in 1980 under the *Pension Benefits Act* and provides protection, subject to specific maximums and exclusions, to Ontario members and beneficiaries of single-employer-sponsored defined-benefit pension plans in the event the plan sponsor becomes insolvent. The PBGF does not cover certain types of small plans (for example, "individual pension plans," which include plans of up to three members); all multi-employer and jointly-sponsored defined-benefit plans; or large plans listed in the regulations to the *Pension Benefits Act* sponsored by named private or government employers, including the Ontario government, several municipalities, General Motors of Canada Ltd., and certain plans of Essar Steel Algoma Inc.; or any defined-contribution pension plans.

The PBGF was intended to be self financing through annual premiums paid by single-employer-sponsored defined-benefit pension plans. Since 1980, the PBGF has collected $1 billion in premiums, and in 2010 it received a $500-million grant from the Ontario government. Over the same period, it paid out $1.4 billion in claims.

Financial Services

The Licensing and Market Conduct Division administers and enforces the requirements of the *Insurance Act*, the *Credit Unions and Caisses Populaires Act*, the *Co-operative Corporations Act*, the *Mortgage Brokerages, Lenders and Administrators Act, 2006*, and the *Loan and Trust Companies Act*. **Figure 2** shows the type and number of individuals and businesses in the regulated financial sectors

Figure 1: Pension Plans Registered with FSCO, as of August 31, 2014

Source of data: Financial Services Commission of Ontario

Type of Plan	# of Plans	# of Members (million)	Description of Plan
Single-employer pension plan (SEPP)	7,194	1.7	A single employer, or several related employers within a corporate group, participate and contribute to the same pension plan. A SEPP can be provided to all or just certain classes of employees. It is usually administered by the plan sponsor (employer) with input from members on certain plans. For defined-benefit plans, the employer is responsible for covering any pension obligations that exceed pension assets. For defined-contribution plans, the pension obligations equal the assets available. About half of the defined-benefit plans are covered by the Pension Benefits Guarantee Fund, whereas the remainder either do not qualify or are exempt.
Multi-employer pension plan (MEPP)	119	0.9	Two or more unrelated employers participate and contribute to the same pension fund. MEPPs are typically established in industries with unionized employees. The employees' collective agreement establishes employers' contributions. The level of member benefits is established by the board of trustees that administers the MEPP. Members' pensions are considered a target and are not fixed; should employers' contributions not be sufficient to cover pension benefits then members' benefits could be reduced. These plans are not covered by the Pension Benefits Guarantee Fund.
Jointly sponsored pension plan (JSPP)	10	1.2	Public sector plans, including municipal and provincial government workers, teachers, and public transit. Decision making for a JSPP is shared by the employer(s) and plan members. This includes all decisions about the terms and conditions of the plan, any amendments to the plan, and the appointment of the plan administrator. If a jointly sponsored pension plan becomes underfunded, both plan members and the employer are jointly responsible for making any required additional contributions to deal with the shortage of funds. No reduction in earned pension benefits is permitted, unless the plan is wound up. These plans are not covered by the Pension Benefits Guarantee Fund.
Total	**7,323**	**3.8**	

that the Licensing and Market Conduct Division registers or licenses.

The Division examines market conduct by investigating all complaints related to the regulated sectors for possible enforcement action, and by conducting on- and off-site compliance audits, or examinations, for certain sectors.

Audit Objective and Scope

Our audit objective was to assess whether FSCO had effective systems and procedures in place for its regulation of pension plans and financial services (insurance, mortgage brokers, credit unions, caisses populaires, loan and trust companies, and co-operative corporations) in Ontario to:

Figure 2: Financial Institutions Regulated by FSCO, as of March 31, 2014*

Source of data: Financial Services Commission of Ontario

Financial Sector	# of Registrants or Licensees	Description of Key Activities Covered and Registration or Licensing Requirements
Insurance companies	339	Automobile insurance, life insurance, health and travel insurance, and property and casualty insurance are covered. All insurance companies, agents, corporate insurance agencies and insurance adjusters operating in Ontario must be licensed with FSCO. However, most insurance companies are federally incorporated and are regulated by the federal Office of the Superintendent of Financial Institutions. FSCO has arrangements in place that permit insurance brokers to be licensed and regulated by their association, the Registered Insurance Brokers of Ontario.
Insurance agencies	5,145	
Insurance brokers	17,875	
Insurance agents	48,213	
Insurance adjusters	1,728	
Mortgage brokerages	1,172	All mortgage-brokering lending activities are regulated by FSCO. All mortgage brokerages, brokers, agents and mortgage administrators are required to be licensed by FSCO.
Mortgage brokers	2,406	
Mortgage agents	7,959	
Mortgage administrators	113	
Credit unions and caisses populaires	129	All credit unions, caisses populaires and co-operative corporations operating in Ontario are required to register with FSCO. The Deposit Insurance Corporation of Ontario is a Crown agency established under the *Credit Unions and Caisses Populaires Act, 1994* to protect depositors of Ontario credit unions and caisses populaires from loss of eligible deposits, and supervise their financial solvency. FSCO's responsibility is limited to investigating complaints on their market conduct.
Co-operative corporations	1,775	
Loans and trusts companies	52	All loans and trust corporations must be federally incorporated and are regulated by the Office of the Superintendent of Financial Institutions. To operate in Ontario, loans and trust corporations must register with FSCO.

* FSCO does not regulate banks, mutual funds or securities handlers in Ontario, which are regulated by the federal Office of the Superintendent of Financial Institutions, Mutual Fund Dealers Associations of Canada, and Ontario Securities Commission respectively.

- ensure compliance with relevant legislation and its own policies established to protect the public interest and to enhance public confidence; and
- measure and report on the effectiveness of its regulatory oversight.

Senior FSCO management reviewed and agreed to our audit objective and criteria.

Our audit work included interviews with FSCO management and staff, as well as reviews and analysis of relevant files and examinations conducted by FSCO; registration, licensing and enforcement databases; and policies and procedures.

We interviewed the chairpersons of FSCO's various pension advisory committees on actuarial services, investments, administration and multi-employer plans. We also met with representatives of the federal Office of the Superintendent of Financial Institutions in Ottawa to discuss their perspective on oversight of federally regulated pension plans. We met with several stakeholders' associations in the mortgage and insurance sectors, as well as with representatives of two mortgage brokerage firms. We also spoke with representatives of the Ontario Securities Commission.

We researched regulatory legislation and operations in several other provinces and jurisdictions, and we engaged an independent expert on pensions.

Our audit fieldwork was conducted from January to July 2014, and we primarily focused on FSCO's activities over the three fiscal years from 2011/12 to 2013/14.

Summary

The growing level of underfunding in defined-benefit pension plans in Ontario is a significant concern (underfunded plans are those that would have insufficient funds to pay full pensions to their 2.8 million members if they were wound up immediately).

As of December 31, 2013, 92% of Ontario's defined-benefit plans were underfunded, compared to 74% as of December 31, 2005. Over the same eight-year period, the total amount of underfunding of these plans grew from $22 billion to $75 billion.

In the wake of the 2008 economic downturn, the government provided temporary solvency funding relief in 2009 to pension plan sponsors, allowing them more time to make additional payments to achieve full funding. In November 2012, additional measures were introduced to extend solvency funding relief because the underfunding of plans had not improved since investment returns remained volatile and interest rates remained low.

FSCO's Superintendent has limited powers under the *Pension Benefits Act* (Act) to deal with administrators of severely underfunded plans, or those who do not administer plans in compliance with the Act. FSCO's federal counterpart, the Office of the Superintendent of Financial Institutions, has the legal authority to terminate a plan, appoint a plan administrator or act as an administrator even if the plan is not terminated, and to require more frequent actuarial valuations of pension plans. FSCO can only prosecute an administrator or must order a plan to terminate before it can then appoint or act as the administrator. In addition, FSCO cannot impose fines on those who fail to file information returns on time; we noted that FSCO took little or no action against late filers.

We concluded that FSCO should make better use of the powers it already has under the Act to monitor pension plans, especially those that are underfunded. Over the last three fiscal years, FSCO conducted on-site examinations of only 11% of underfunded plans on its solvency watch list; at this rate, it would take about 14 years to examine them all. As of September 2014, it was still in the process of finalizing its risk-based methodology for selecting higher-risk plans to examine. The examinations FSCO did conduct did not adequately cover significant areas, such as whether investments complied with federal investment rules required for pension plans. In addition, FSCO's efforts and processes to monitor the $19.2 billion in investments managed by administrators of defined-contribution pension plans were weak.

The information provided by plan administrators and made public by FSCO would be of little use to plan members for assessing and comparing the performance and administration of their pension plans with other plans or relevant benchmarks; nor would members find it of value in assessing whether FSCO had adequately protected their interests.

Although the trend in claims has improved, it is uncertain whether the province's Pension Benefits Guarantee Fund (PBGF), designed to protect members and beneficiaries of single-employer defined-benefit plans in the event of employer insolvency, is itself sustainable. The PBGF was intended to be self-financing through annual premiums charged to pension plans; since the plan's inception in 1980, however, the government has provided a total of $855 million in loans and a grant to help cover claims payouts of $1.4 billion. The PBGF has no legal obligation to pay claims in excess of its available assets.

A $500-million grant in 2010, along with increases in premium rates introduced in 2012, have helped the PBGF's financial position; it had a $375-million surplus as of March 31, 2014. However, in the event of another economic downturn, this surplus would be quickly exhausted given that the cumulative deficits of pension plans covered by the PBGF as of March 31, 2014, were almost $28.9 billion. This represents an increase of more than 400% since 2008—even though the number of pension plans covered actually dropped by 19% since then.

With respect to the Licensing and Market Conduct Division's (Division) oversight of regulated financial service sectors, we noted several areas that it needs to address, particularly to reduce investor risk and protect consumers:

- ***Minimal oversight of co-ops.*** FSCO oversees the registration of co-operative corporations (co-ops), which can raise millions of dollars from investors for ventures such as renewable energy initiatives. Over the last three years, FSCO gave 57 approvals for co-ops to raise up to $371 million. However, it does no criminal background checks of key members before a co-op is registered and begins to raise money; nor does it conduct ongoing monitoring of their activities. Furthermore, it cost FSCO over $500,000 annually to review and approve co-op offering statements, but FSCO can charge only $1,000 in total fees for this service.
- ***Monitoring of life insurance agents weak.*** Weaknesses in FSCO's online licensing system allow life-insurance agents to hold active licences without having entered proper information about whether they have insurance for errors and omissions (to cover client financial losses arising from agent negligence or fraud). FSCO does not verify whether an agent's errors and omissions insurance is valid, and relies on insurance providers to notify it of cancelled policies—even though it had no formal arrangements with the providers to do so. FSCO has also renewed licences of agents who were disciplined by other financial service regulators, those who declared bankruptcy, and those with criminal records, because it did not investigate their applications.
- ***Delays in handling complaints.*** The Division incurred significant delays over several serious complaints and the investigations ended in weak enforcement action. For instance, serious allegations of fraud and forgery against licensed agents took years to investigate and the agents' licences remained active during the investigation.
- ***Division proactive examinations limited to the mortgage brokerage sector.*** The Division does not examine other regulated financial service sectors unless an investigation has been initiated due to a complaint. In addition, the Division did not have adequate procedures and information-sharing arrangements with other financial service regulators to ensure FSCO is notified immediately when agents are disciplined. Even when FSCO was aware of disciplinary action against an agent, it did not routinely initiate its own proactive examination into the business practices of these agents.

In addition, we observed that the large numbers of registrants and licensees in several regulated financial services industries, including mortgage brokerages and insurance, may justify these industries assuming greater responsibility for self-oversight. This could include establishment of self-regulation and consumer-protection funds, as is currently the case with many other similar self-regulated service industries. However, FSCO would have to seek legislative changes in consultation with the Ministry of Finance and government officials for this to occur.

Detailed Audit Observations

Pensions

Increasing and Significant Underfunding of Defined-benefit Pension Plans

As of December 31, 2013, the pension incomes of approximately 3.4 million people in Ontario depended on defined-benefit pension plans, which had assets of $420 billion. For the pension plans to pay benefits to members on retirement, the assets of the plan must be sufficient to meet the pension promise, also known as the pension liability.

A plan's investment assets are composed of regular contributions by the employer and, when applicable, the employees, plus income made on investing the assets, less benefits paid out to pensioners and expenses to administer the plan. Investment assets are susceptible to fluctuations in returns, and to the number of people contributing to the plan and the number receiving benefits.

Pension liability is affected by interest rates (used to calculate the present value of pension amounts payable), by the number of members, and by how long the members are expected to live and continue to collect pensions. As a result, it is important to regularly monitor defined-benefit plan assets, employer and employee contributions, and the predicted pension liability to ensure there will be sufficient funds to pay out benefits when required.

A defined-benefit pension plan has a solvency deficiency, or funding deficit, when it is underfunded and does not have enough in assets to pay its pension liability if the plan were to wind up immediately. The *Pension Benefits Act* requires the employer, as well as employees for jointly sponsored pension plans, to increase contributions by making additional payments for up to five years to eliminate the solvency deficiency and make the plan fully funded. Similarly, should a pension plan have a surplus, the plan administrator can ask to make lower contributions.

Since the 2008 economic downturn in Ontario, the overall solvency deficiency of active defined-benefit pension plans has worsened, as follows:

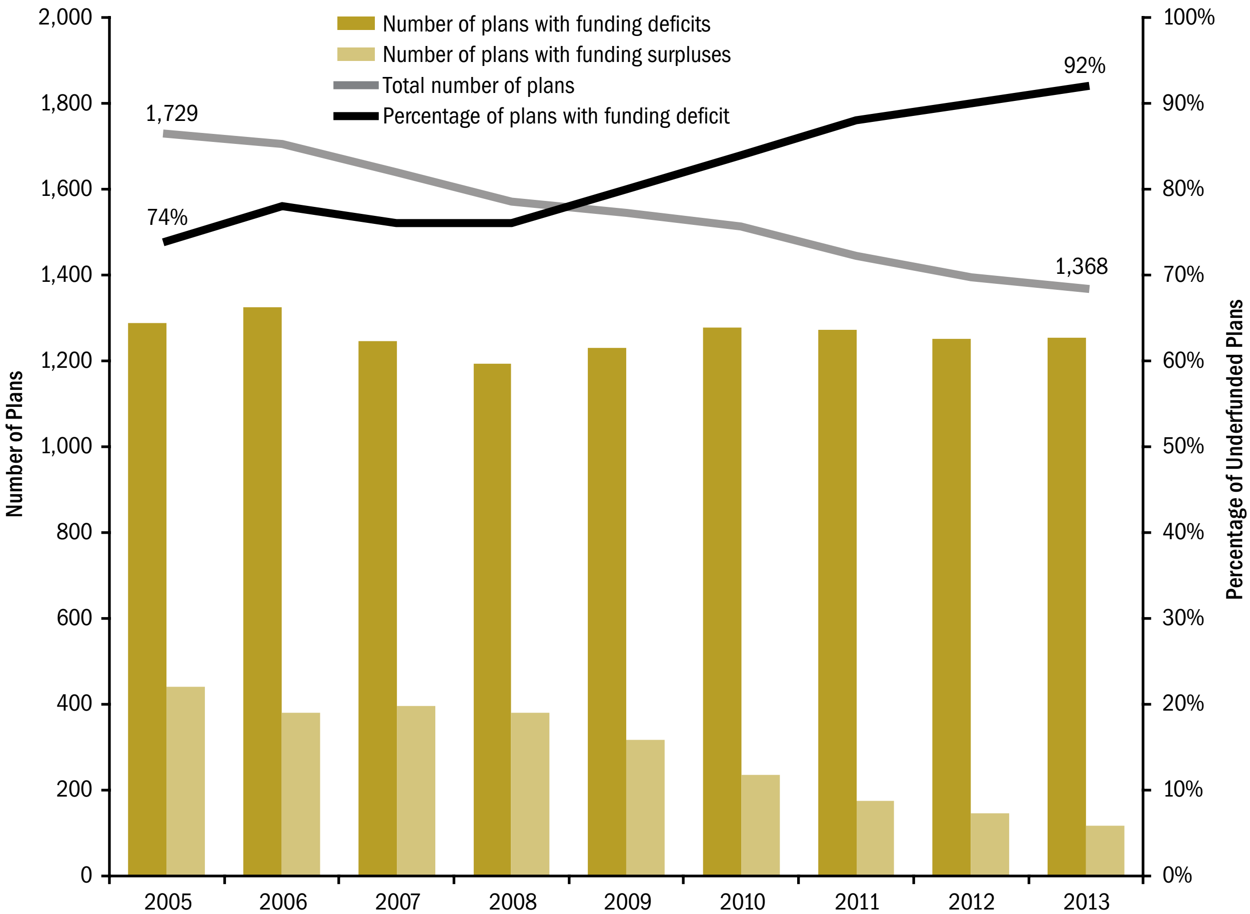
- As of December 31, 2013, 92% of defined-benefit plans were underfunded and did not have sufficient assets to pay members their full pensions if the plans were wound up immediately, as illustrated in **Figure 3**. That percentage is up from 74% for the year ended December 31, 2005 (the earliest year for which FSCO could provide information). The 92% of defined-benefit plans that are currently underfunded have more than 2.8 million members.
- As **Figure 4** indicates, the total amount of underfunding of defined-benefit pension plans in Ontario has grown from $22 billion as of December 31, 2005, to $75 billion as of December 31, 2013. The total liability of these plans as of December 31, 2013, was $370 billion, and total assets were $295 billion, with the difference—$75 billion—being the underfunding. The $75 billion breaks down as follows: $33 billion for single-employer plans; $16 billion for multi-employer; and $26 billion for jointly sponsored.
- As **Figure 5** indicates, all types of defined-benefit plans—single-employer, multi-employer and jointly sponsored plans—have had the amount of their underfunding increase since the 2008 economic downturn.

In the wake of the economic downturn, the government introduced measures in 2009 providing temporary solvency funding relief to pension plan sponsors, allowing them more time to make additional payments to achieve full funding. They could elect to defer by one year the new additional payments required in the first valuation after September 30, 2008. In addition, all pre-existing additional payments owed by a plan sponsor could also be consolidated and paid over a new five-year schedule. Any new solvency deficiency could also be paid over an additional five years if that was approved by members of the pension plan. Plan administrators could elect any or all of the solvency relief funding options without approval from FSCO. There were 471 pension plans, or 30% of all active defined-benefit pension plans, that elected solvency funding relief in 2009.

By 2012, the solvency deficiency of defined-benefit pension plans from 2008 had not improved because investment returns continued to be volatile and interest rates remained low, so the government extended the solvency funding relief by introducing additional measures on November 1, 2012. The extension covered the first actuarial valuation report on or after September 30, 2011, and before September 30, 2014. The new measures allowed pension plan administrators to consolidate their existing remaining additional solvency payments into a new five-year schedule and allowed any newly filed solvency deficiency to be paid off over

Figure 3: Number and Percentage of Active Defined-benefit Plans with Funding Surpluses and Funding Deficits, years ending December 31, 2005–2013*

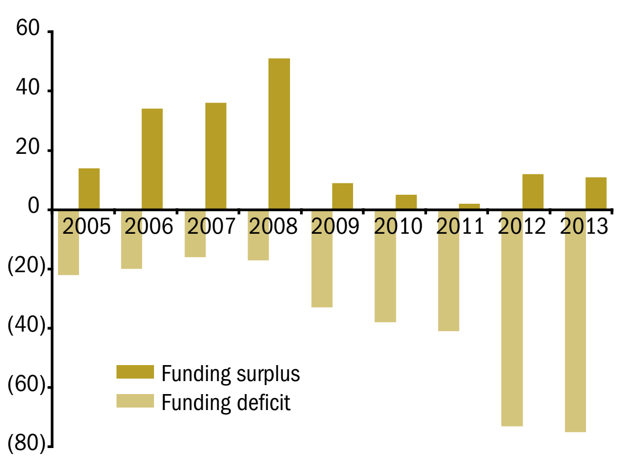
Source of data: Financial Services Commission of Ontario



* Excludes individual, closed and frozen defined benefit pension plans. Frozen plans are those where members are no longer accruing future benefits.

Figure 4: Total Amount of Funding Surplus and Funding Deficit for All Active Defined-benefit Plans, years ending December 31, 2005–2013, ($ billion)

Source of data: Financial Services Commission of Ontario



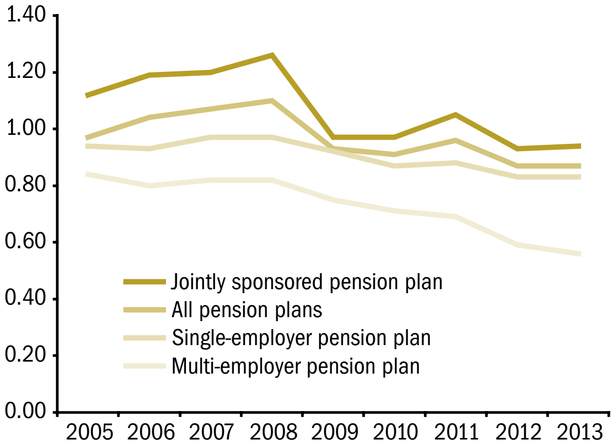
10 years, subject to the consent of the pension plan's members. In total, 215 pension plans elected 2012 solvency relief; of these, 134 had also elected solvency relief in the previous round.

Sustainability of the Pension Benefits Guarantee Fund

The Pension Benefits Guarantee Fund (PBGF) was initially intended to be self-financing through annual assessment fees charged to eligible single-employer defined-benefit pension plans. While the PBGF is seemingly in a better financial position now than it was before the 2008 economic downturn as a result of changes since made by

Figure 5: Weighted Average Solvency Ratio of Active Defined Benefit Pension Plans, for the years ended December 31, 2005–2013*

Source of data: Financial Services Commission of Ontario



* FSCO uses a solvency ratio to express the extent a defined-benefit pension plan is funded. For instance: a plan that is fully funded is represented by 1.00; a plan in deficit and funded at only 85% is represented by 0.85; and a plan with a funding surplus of 20% is represented by 1.20.

the government (discussed later), its financial risk exposure has actually increased significantly. In March 2014, the PBGF had a $375-million surplus to cover any claims, up from a $102-million deficit in March 2008. However, as **Figure 6** shows, in 2008 there was a cumulative $6.6-billion solvency deficiency for 2,258 pension plans covered by the PBGF; as of March 31, 2014, this cumulative solvency deficiency had increased by more than 400%, to almost $28.9 billion, covering only 1,834 plans, 19% fewer than in 2008.

Under the *Pension Benefits Act*, the PBGF liability to pay claims related to insolvent pension plans is limited to only the assets of the fund. The Ministry of Finance may, at the government's discretion, make a grant or a loan to the PBGF to help it meet any shortfall, although the Act does not require it to do so. **Figure 7** shows government loans and a grant to the PBGF since March 31, 2004, to help it cover large corporate pension plans that were no longer viable. Since its inception in 1980, the PBGF has required loans and a grant from the Ontario government totalling $855 million to cover all eligible claims. In addition, the government has provided financial support directly to large corporations experiencing financial difficulties that involved pension plans with large solvency deficiencies.

The PBGF has paid $1.4 billion for 242 claims since its inception and as of March 31, 2014, it had outstanding loans payable to the province of $220 million. Of the $1.4 billion in claims, 54% ($759 million) was for the pension plans of two companies: $375 million to the then-Algoma Steel in 2004/05, and $384 million to Nortel in 2011/12. Excluding these two claims, the average for the remaining 240 claims was about $2.7 million each.

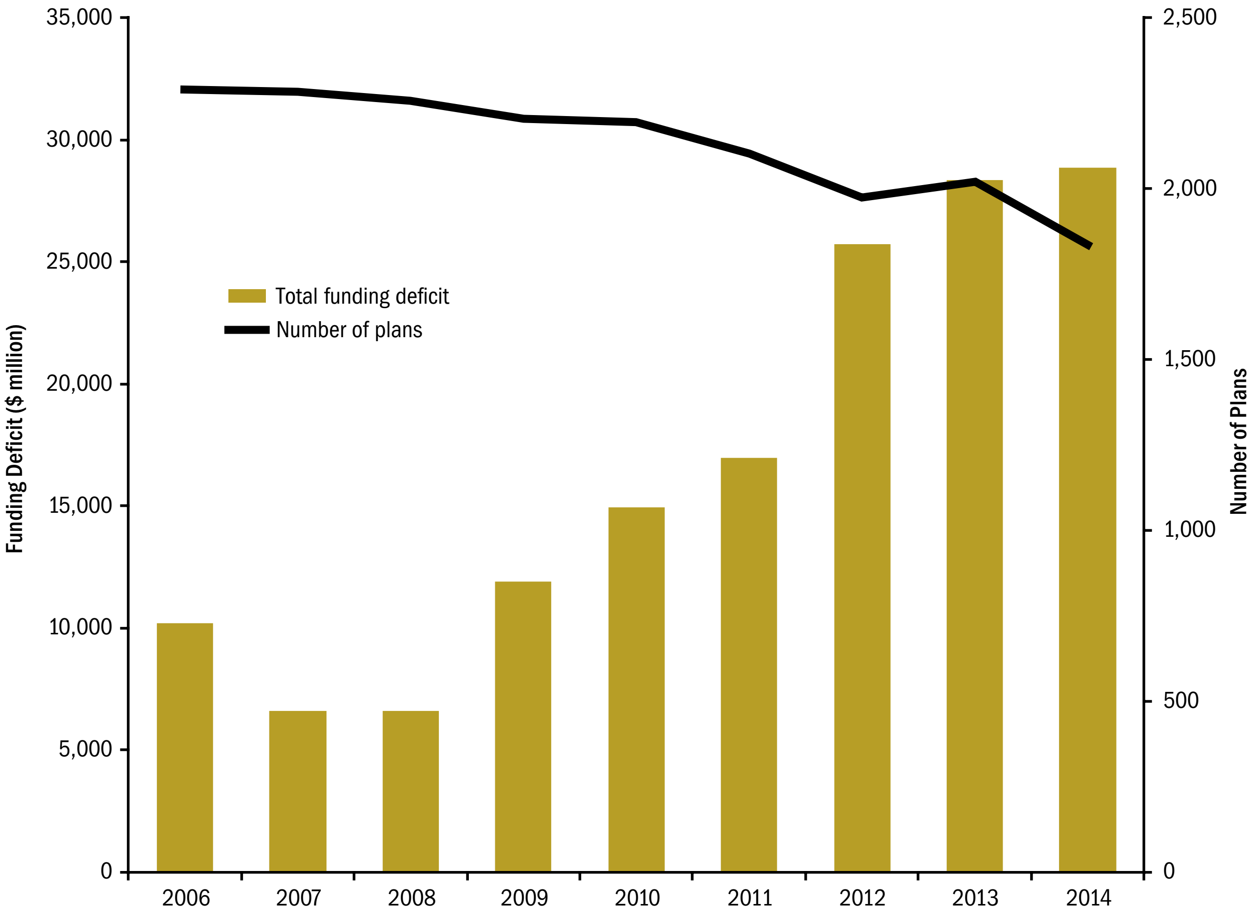
As of August 31, 2014, there were 15 employers who each sponsored pension plans with solvency deficiencies greater than $200 million and solvency ratios ranging from 0.69 to 0.93, that were covered by the PBGF. Should any of these plans be required to wind up, the negative impact would be substantial on thousands of plan members and the PBGF. In addition, there were 25 single-employer, multi-employer and jointly sponsored pension plans that each had a solvency deficiency greater than $200 million, and solvency ratios ranging from 0.53 to 0.94, that were not covered by the PBGF and that would have a substantial impact on thousands of members should their plans be required to wind up.

There have been several studies since 2008 that have questioned the sustainability of the PBGF:

- The report of Ontario's 2008 Expert Commission on Pensions (the Arthurs Report), questioned the continuation of the PBGF, recommending that "[t]he Ministry of Finance or some other agency, either alone or in co-operation with other Canadian pension authorities, should initiate a study of possible alternatives to the Pension Benefits Guarantee Fund. …On the basis of the findings of that review, the government should determine whether to continue, amend, replace or discontinue the PBGF."
- Based on a recommendation made in the Expert Commission on Pensions report, the Ministry of Finance commissioned a study by an independent consultant in 2010 to

Figure 6: Number of Pension Plans and Total Funding Deficit of All Plans Covered by the PBGF, for the years ending March 31, 2006–2014

Source of data: Financial Services Commission of Ontario



evaluate the sustainability of the PBGF. The study concluded that "currently, the PBGF has insufficient funds to cover the anticipated 2010 claims. If continued, the PBGF will either need to build up reserves and/or secure future external funding to cover future catastrophic claims. The amount of reserves or funding required will depend on future assessment levels and the desired degree of confidence with which future claims will be covered by assessments."

Effective January 1, 2012, changes to the Pension Benefits Act were made to increase PBGF revenues. Annual assessments were increased, with the base fee per Ontario plan member raised to $5 from $1; the maximum fee per Ontario plan beneficiary in unfunded pension plans was raised to $300 from $100; the $4 million assessment cap for unfunded pension plans was eliminated; and a minimum assessment fee of $250 was established for all defined-benefit pension plans. As shown in **Figure 7**, the annual assessment revenue increased almost $60 million in the fiscal year 2012/13 following these changes.

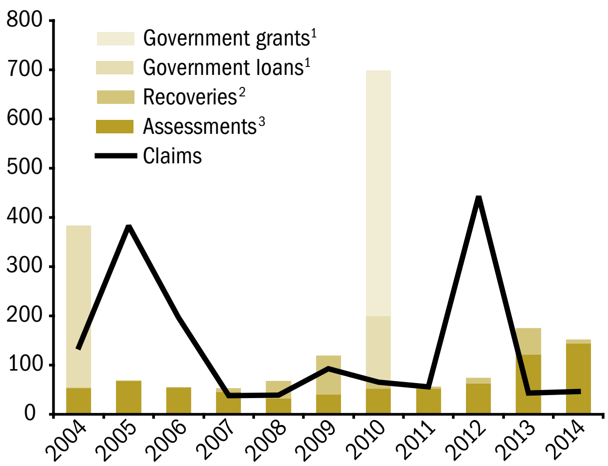
In addition, changes were made to the *Pension Benefits Act* to reduce future claims costs for pension plans with a wind-up date on or after December 8, 2010. For instance, the exclusion period changed from three years to five years before a new pension plan qualified for coverage by the PBGF.

- The February 2012 Commission on the Reform of Ontario's Public Services (the Drummond Report) also questioned the continuation of the PBGF. The Drummond Report found "[t]he Fund is no longer sustainable in its current form as it presents a large fiscal risk for the province in the event of another economic downturn," and recommended that "the province either terminate the [PBGF] or explore the possibility of transferring it to a private insurer."

- A March 2012 report by the Fraser Institute observed that "Although Ontario is the only Canadian province with a fund guaranteeing private sector defined-benefit pension plans, the problems it is experiencing are similar to those of comparable funds in other jurisdictions, including the United States and United Kingdom."

Figure 7: PBGF Revenues and Claims, for the years ending March 31, 2004–2014 ($ million)

Source of data: Financial Services Commission of Ontario



1. A non-interest bearing loan of $330 million was received from the Government of Ontario on March 31, 2004 to assist the PBGF in meeting claims related to the wind-up of two Algoma Steel pension plans. Between May 2003 and May 2004, the PBGF paid claims of $460 million related to Algoma Steel pension plans. (In 2007–2011, the PBGF recovered $85 million, resulting in a net claim of $375 million relating to Algoma Steel.) Interest-bearing loans totalling $130 million were received from the Government of Ontario in August 2009 and January 2010 to support the PBGF for claims due to the 2008 economic downturn. A $500-million grant was received in March 2010 from the Government of Ontario to pay off the $130 million in loans received in 2009 and 2010 and to support the PBGF in meeting claims relating to Nortel pension plans.
2. PBGF claims are paid to pension plans based on the submission of an interim windup report. Pension plans submit a final windup report once the pension plan has completed payouts to all members. Funds that are remitted back to the PBGF for the overpayment of claims are called recoveries.
3. The assessments paid by pension plans increased effective January 1, 2012, increasing revenues by almost $60 million from 2012 to 2013.

The Fraser Institute report noted that the U.S. Pension Benefit Guarantee Corp. operated at a $27-billion deficit in 2011, its largest deficit since its inception in 1974. The UK's Pension Protection Fund acknowledged in 2010 that it did not have sufficient financial resources to pay existing levels of compensation and would not be fully funded until at least 2030.

RECOMMENDATION 1

In view of the significant increasing underfunding of defined-benefit pension plans in Ontario, the Financial Services Commission of Ontario should conduct an analysis of the reasons for this increase, the potential for plans to recover based on a variety of predictions of economic growth in the province over the next several years, and the financial exposure to the province should the underfunding situation not improve in the next few years.

It should use this information to identify and recommend strategies and changes to the legislation that could help to inform and mitigate the financial risk to sponsors and members of pension plans, as well as to legislators and taxpayers.

FSCO RESPONSE

FSCO agrees that it may be useful to conduct additional analysis and to make this information available to the government should it wish to use it in developing pension policy. FSCO would continue to co-operate fully and respond to requests from the government for advice on pension funding issues. It should be noted that under the *Pension Benefits Act* there is no direct financial risk to the province from underfunded pension plans apart from as a sponsor of the Public Service Pension Plan and co-sponsor of the Ontario Teachers' Pension Plan and the OPSEU Pension Plan.

FSCO monitors emerging trends relating to the health of pension plans in Ontario. For example, in 2014 it published its tenth annual

Report on the Funding of Defined Benefit Pension Plans in Ontario. This report provides relevant information on the current status and the trends relating to, for example, the funded status of pension plans, the use of funding relief provisions and their impact, and the investment of pension funds. On a quarterly basis, FSCO also estimates and analyzes the solvency status of pension plans.

RECOMMENDATION 2

The Financial Services Commission of Ontario should assess the Pension Benefits Guarantee Fund's (PBGF) financial risk exposure to potential claims and its continuation as an insurer of single-employer defined-benefit pension plans, and it should use this information to recommend further possible changes to the *Pensions Benefits Act* and regulations to address the sustainability of the PBGF.

FSCO RESPONSE

FSCO monitors the PBGF on a regular basis by producing reports that estimate current PBGF inflows and outflows. Moreover, FSCO estimates potential claims by monitoring the status of pension plans of companies that are under financial distress, including those under *Companies' Creditors Arrangement Act* (CCAA) proceedings and receivership. FSCO will seek ways to enhance its analysis of the PBGF financial exposure and to make available its analysis to the government should it wish to use it in developing pension policy.

Limited Powers of the Superintendent

FSCO's responsibility regarding pension plans is to ensure members' future benefits are secure. Its activities include:

- registering new pension plans and pension plan amendments;
- processing required filings from plan administrators, including annual information returns, actuarial valuation filings, investment information returns, and financial statements;
- monitoring pension plans and pension funds to ensure they are being administered, invested and funded in compliance with the *Pension Benefits Act*;
- issuing Superintendent Orders, such as for the involuntary wind-up of a pension plan due to the insolvency of a plan or employer; and
- responding to inquiries and complaints from pension plan members, investigating alleged breaches of the *Pension Benefits Act* and taking enforcement action when required.

Each pension plan must have a plan administrator, who may also be the employer sponsor, and is responsible for statutory funding contributions; administration and payment of benefits to members; managing the investment of plan assets in compliance with relevant laws; annual reporting to members; and responding to member inquiries. Plan administrators may delegate some or all of these responsibilities to third-party service providers such as actuaries, accountants, lawyers, pension plan consultants, investment managers, trust companies and benefits administration companies. The pension funds are held in trust accounts maintained by trust or insurance companies appointed by the plan administrator. The plan administrator has no access to funds held in trust accounts, although the plan administrator may make investment decisions involving the funds.

We noted the Superintendent has limited powers under the *Pension Benefits Act* to take action against plan administrators of severely underfunded pension plans and plans not being administered in compliance with the Act, short of prosecution or ordering the wind-up of a plan.

Powers to Appoint a Plan Administrator

FSCO prepares a monthly internal solvency watchlist report that lists all defined-benefit pension plans with solvency concerns (generally when the ratio of pension assets to liabilities is at less than 85% based on the most recent actuarial valuation report filed by each plan administrator). **Figure 8** shows that as of December 31, 2013, the solvency watch list included 696 pension plans with solvency concerns representing 1.8 million active and retired members, with the amount of the underfunding totalling approximately $65 billion. About 45% of these plans had solvency ratios that had deteriorated to less than 0.70.

When a pension plan is not being administered in compliance with the Act—for example, required documents have not been filed with FSCO, required contributions have not been made, or federal investment rules are not being met—the Superintendent can issue an order directing the plan administrator to take specific actions for the plan to comply with the Act. If the plan administrator does not comply with the order, the Superintendent can initiate prosecution against the plan administrator under the *Provincial Offences Act*.

The Superintendent has no power to appoint a new administrator to a pension plan, even when the plan administrator has not met its obligations, unless the plan is being wound up. A plan can be wound up by order of the Superintendent under the following circumstances: the employer stops making required pension plan contributions, including additional payments to cover solvency deficiency; the employer becomes bankrupt; a significant number of pension plan members' employment is terminated; closure or sale of the employer's business; or the liability of the PBGF is likely to substantially increase if the pension plan is allowed to continue operating.

In comparison, the federal Office of the Superintendent of Financial Institutions (OSFI) has a number of discretionary powers to address specific pension plan solvency issues. The objective is to intervene as early as possible to minimize problems before they escalate and to reduce the risk of loss to pension plan members.

OSFI has developed a five-stage rating system that determines the level of intervention required, as follows:

- *Stage Zero: No significant problems.* Ongoing monitoring of the plan continues.
- *Stage One: Early warning.* Deficiencies in the plan's financial position are identified and it could be placed on a watch list. OSFI increases monitoring of the plan and may require additional relevant filings.
- *Stage Two: Risk to solvency.* OSFI intensifies its supervisory interventions, requiring that the administrator take actions such as submitting a revised or early actuarial report or holding meetings with plan members.
- *Stage Three: Future solvency in serious doubt.* OSFI escalates its intervention because of immediate threats to plan members' benefits. OSFI can remove the plan administrator and appoint a replacement; designate an actuary to prepare a report for funding purposes;

Figure 8: Funding Deficits of Pension Plans on FSCO's Solvency Watch List, as of December 31, 2013

Source of data: Financial Services Commission of Ontario

Solvency Ratio	# of Plans	Active Members	Retired and Other Members	Total Members	Plan Assets ($ million)	Liability to Members ($ million)	Funding Deficit ($ million)
<0.40*	5	153,755	240,569	394,324	1,810	5,264	**(3,454)**
>= 0.40 <0.55	26	99,957	122,652	222,609	7,998	16,415	**(8,417)**
>= 0.55 <0.70	281	166,155	187,822	353,977	26,087	39,973	**(13,886)**
>= 0.70 <0.85	384	457,029	412,917	869,946	126,940	166,412	**(39,472)**
Total	**696**	**876,896**	**963,960**	**1,840,856**	**162,835**	**228,064**	**(65,229)**

* One plan with a solvency ratio of 0.34 accounts for the majority of this category. FSCO has prosecuted the plan administrator and also entered into two negotiated agreements to reduce the funding deficit.

bring action against the administrator; or terminate the plan.

- *Stage Four: Permanent insolvency.* OSFI facilitates the wind-up of the plan.

In December 2010, an amendment to the *Pension Benefits Act* was passed that would authorize the Superintendent to terminate a plan administrator and either appoint a new one or allow the Superintendent to act as the plan administrator. However, the amendment still requires proclamation by the Lieutenant Governor for this new power to come into force, and for the government to establish a regulation that prescribes the circumstances when the Superintendent can terminate a plan administrator. No date has been set for when these preconditions will be met.

More Frequent Actuarial Valuations and Review of Valuations of Defined-benefit Pension Plans Needed to Assess Funding Status

Periodic actuarial valuations determine whether a plan has sufficient assets to fund its expected pension liability obligations to its members. Valuation of a pension plan's assets and liabilities can change significantly from year to year, since growth in pension assets depends on investment returns, interest rates, and the extent of benefit payments to retirees, who are generally living longer.

During the 2008 economic downturn, pension assets invested in equity markets dropped in value by as much as 35% in a matter of weeks. As well, the extended period of low interest rates since the downturn has further reduced investment returns well below what they have been historically and increased pension liabilities. Allowing a long time between actuarial valuation reports poses risks to pension plan members and to FSCO's monitoring of whether plans have solvency deficiencies.

Under the *Pensions Benefits Act*, plan administrators of defined-benefit plans must file actuarial valuation reports every three years (triennial valuations) if their plan does not have a solvency concern, such as when the solvency ratio is 0.85 or higher, or annually if the solvency ratio is lower. FSCO does not have the power to order an interim actuarial valuation of a pension plan. As of December 31, 2013, there were 816 defined-benefit plans, or 60% of all active plans with solvency concerns, that were required to file actuarial valuation reports annually.

Federal pension legislation requires more frequent filing of actuarial valuation reports. Plans funded at less than 120%—a significantly higher threshold than the 85% in Ontario—are required to file every year, as opposed to every three years. This allows for more accurate and timely reporting on the funding status of pension plans. If Ontario were to require actuarial valuation reports using a funding level of 120%, all but 33 active defined-benefit pension plans would be required to file annually as of December 31, 2013.

Up until the fall of 2011, FSCO carried out reviews of approximately 30% of actuarial reports received each year to ensure plan provisions had been properly reflected and that data, methods and assumptions used to determine the financial positions and sponsor contribution requirements of the plan met FSCO's expectations. For instance, actuaries can use their judgment for assumptions in predicting long-term mortality and interest rates. Over the past five years, FSCO received approximately 1,700 actuarial valuation reports annually. However, FSCO now carries out detailed reviews of only a small number of actuarial reports each year on a sample basis. FSCO no longer formally tracks the number of reviews it performs every year, and does not report internally or externally the results of these reviews. In contrast, we noted that the federal OSFI publicly reports the number of detailed actuarial valuation reviews completed yearly, as well as their observations from the reviews. By communicating this information, OSFI helps educate plan sponsors and actuaries on addressing these findings before they submit their reports for review.

Non-compliance with Statutory Filing Requirements by Pension Plans

The *Pension Benefits Act* requires pension plan administrators to regularly file with FSCO key information on the plan, including its funding status, sponsor contributions, investment returns and activities, and member pension obligations. **Figure 9** provides a description of the required filings and their due dates.

To effectively monitor pension plans, FSCO must ensure it receives statutory filings on a timely basis, or take action when they are not received. **Figure 10** shows that as of May 2014, 1,384 pension plan administrators had not submitted one or more statutory filings on their due dates and were past due for over one year. FSCO had taken action on only 13% of these cases, or 176 plans, and the action taken was limited to sending a letter to the plan administrator requesting compliance with filing requirements. No action was taken on 1,208 plans, including 127 plans that had pension assets of more than $1 million.

FSCO levies no penalties on administrators who file persistently late. FSCO told us it has taken legal action against plan administrators only twice—after the plans fell years behind in filings—and the courts imposed fines in these cases. However, FSCO's efforts to prosecute these administrators were labour-intensive and costly.

FSCO has had the power to impose administrative monetary penalties (AMPs) in the mortgage sector since 2008, but not on pension plan administrators. In 2013/14, there was a 95% compliance rate by mortgage brokers for submitting statutory filings. FSCO has been authorized to issue AMPs in the insurance sector since 2013, and recommended in 2010 to the Ministry of Finance that it be granted the authority to issue AMPs in the pension sector. However, no action has so far been taken by the Ministry of Finance to propose the necessary changes to the *Pension Benefits Act*.

Figure 9: FSCO Filing Requirements by Pension Plan Administrators, as of March 31, 2014*

Source of data: Financial Services Commission of Ontario

Name of Filing	Frequency Filed	Type of Pension Plans that File	Description
Annual information return	Annually	All plans	Contains general information on the pension plan including the name of the plan sponsor, plan administrator and details on the number and status (active, retired) of members.
Investment information summary	Annually	Defined benefit	Provides details on the change in asset values year-over-year including the asset mix of investment assets
Actuarial funding valuation report and actuarial information summary	Normally filed triennially; however filed annually for plans with a solvency ratio below 0.85 on their most recently filed actuarial funding valuation report	Defined benefit	The valuation report is prepared by an accredited actuary in accordance with the Canadian Institute of Actuaries Standards of Practice, and identifies the main assumptions used and determines the plan's solvency ratio, which is the surplus or deficit of pension assets to the predicted liability for future retirement benefits. The information summary details the overall plan assets and liabilities, solvency ratio and the amount of any additional payments that the plan sponsor needs to make into the pension plan.
Pension fund financial statement	Annually	All plans	The financial statements of the pension plan. All pension plans with more than $3 million in assets must file audited financial statements.
Pension Benefits Guarantee Fund (PBGF) assessment certificate	Annually	Defined benefit	Calculates the fee that a pension plan needs to pay into the PBGF based on the size of the pension plan's funding deficit and number of members in the pension plan.

* Filings are in accordance with the requirements of the *Pension Benefits Act* and regulations.

Figure 10: Number of Delinquent Pension Plan Administrators that Have Not Submitted a Required Filing for Over One Year, as of May 2014

Source of data: Financial Services Commission of Ontario

	No Action Taken by FSCO	Minimal Action Taken by FSCO[1]	Total
Annual information return	127	**39**	**166**
Investment information summary	14	**7**	**21**
Actuarial funding valuation report and Actuarial information summary	40	**29**	**69**
Financial statements	1,014	**98**	**1,112**
PBGF assessment certificate	13	**3**	**16**
Total	**1,208**	**176**	**1,384[2]**

1. FSCO sent follow-up letters to the plan sponsor.
2. 188 pension plans included in these totals have been counted twice since they had more than one filing overdue. As a result, 1,196 pension plan administrators had at least one filing overdue for over one year. In addition, 938 of 1,384 pension plans, or 68% of the total, are defined-contribution plans.

RECOMMENDATION 3

To ensure the Superintendent has sufficient powers, authority and information to effectively monitor the administration and solvency of pension plans, the Financial Services Commission of Ontario should make changes to its policies and procedures, and, where necessary, seek changes to the *Pension Benefits Act*, to:

- provide it with similar powers to that of the federal Office of the Superintendent of Financial Institutions, including powers to terminate, appoint and act as a plan's administrator;
- establish a staged approach for earlier monitoring and supervision of pension plans that have solvency deficiencies;
- increase the Superintendent's power to order a plan administrator to provide an actuarial valuation report, particularly when a plan has a solvency deficiency, and introduce a program that regularly assesses the reasonableness of assumptions used in these reports; and
- take more proactive follow-up action against plan administrators that do not submit statutory filings on time, and acquire powers to impose penalties for late filing.

FSCO RESPONSE

FSCO will undertake to provide advice to the government to identify those circumstances that would require the Superintendent to terminate an administrator or appoint or act as an administrator in an ongoing plan.

FSCO agrees with this recommendation. FSCO has undertaken the development and implementation of a risk-based regulation framework that will provide for identification of pension plans which may be at risk and provide for a more intensive escalating staged-level of monitoring and supervision of those plans.

Legislative changes that would broaden the Superintendent's power to order actuarial valuation reports to be prepared and to order changes in actuarial assumptions are awaiting the development of supporting regulations. FSCO continues to look for ways to further enhance its program for assessing the reasonableness of actuarial assumptions.

FSCO's introduction of mandatory electronic filing in 2013 and the implementation of the Pension Oversight Unit has resulted in a significant decrease in the number of late filings and removal of the backlog of outstanding late filings. FSCO agrees that the introduction of administrative monetary penalties (AMPs) would be an effective tool. FSCO has legislative authority to use AMPs in other sectors it regulates and will provide advice to the government to identify those circumstances where AMPs would be an effective regulatory tool.

Examination of Plans

More Frequent and Thorough Examinations and Enforcement Action Needed

The *Pension Benefits Act* gives FSCO the power to conduct examinations of and inquiries into pension plans. However, we noted that there were few examinations compared to the number of pension plans it regulates, and the examinations did not result in enforcement action. In addition, FSCO had no authority to request financial information, such as a corporation's financial statements, from an employer that sponsors a pension plan that would allow it to assess the financial health of the employer to determine if contributions to the plan were at risk before bankruptcy occurs.

FSCO conducted 50 pension plan examinations annually in each of the last three fiscal years. Examinations focused on the plan administrators' governance, administration, funding and investment practices.

The vast majority of plans selected for examination were defined-benefit and hybrid plans, and only 14 defined-contribution plans were examined during this period. At this rate, we calculated it would take FSCO well over 100 years to examine the more than 7,300 plans it regulates, and about 14 years if it just limited its examinations to all plans on its solvency watch list. For instance, only 11% of the plans on the solvency watch list as of December 31, 2013, had been examined over the previous three fiscal years.

FSCO's investment, actuarial and technical consulting units chose the plans to examine. Plans were chosen mainly because they had a record of investment concerns or late filings. In 2012, FSCO began implementing a new risk-based regulation of pension plans in Ontario, although this had not been finalized as of September 2014. The proposed framework aims to improve FSCO's overall effectiveness in monitoring key pension risks and take appropriate regulatory actions to address these risks to protect the plan beneficiaries. As part of this, FSCO is developing a new selection approach and assessment process to identify high-risk pension plans for in-depth monitoring focused on five risk areas: funding, investment, administration, governance and sponsor/industry.

The plan administrator is responsible for ensuring that pension contributions are invested in accordance with the *Pension Benefits Act*, which requires compliance with the federal investment rules contained in the *Pension Benefits Standards Act*. For example, the pension plan may not invest more than 10% of its assets in any individual investment and cannot own more than a 30% interest in any one investment unless certain undertakings are filed by the plan administrator with FSCO. The rules also require that pension plan administrators develop a written Statement of Investment Policies and Procedures (SIPP), which is typically approved by the board of directors of the plan, and the SIPP is to be reviewed annually. The SIPP requires an appropriate asset mix, rate of return expectations, level of diversification and risk tolerance for the plan.

Starting in 2006, the *Pension Benefits Act* required defined-benefit pension plan administrators to provide a yearly Investment Information Summary, outlining current asset mix, investment performance, and total administrative and investment fees paid by the plan. The plan administrator is also required to attest to the plan's compliance with federal investment rules in the Summary. The intent of the Summary is to allow FSCO to identify irregularities or significant breaches of federal investment rules, unusual investment performance or unsuitable investment mixes. However, plan administrators are not required to include in the Summary a detailed listing of their investments, and financial statements filed by plan administrators provide some, but not all, information needed for FSCO to ensure compliance with federal investment rules without initiating a full on-site examination. Given the findings of FSCO's limited examinations, such reporting may be warranted, at least for riskier pension plans.

FSCO conducts both on-site plan examinations and reviews of annual filings. We noted the on-site plan examinations commonly identified weaknesses in investment practices. For example, there were cases where no SIPP was in place, the SIPP had not been reviewed for several years and/or the SIPP had not been updated by the administrator to reflect current investment practices. FSCO had not taken any enforcement action against any plan sponsor based on the examination results, even though the plan administrators had provided an attestation in their Investment Information Summary that they complied with federal investment rules.

FSCO's on-site review of investments during examinations was generally limited to reviewing plan policies, and we noted that there was no sampling of individual investments in plans to test for their compliance with federal investment rules. As an example of why FSCO should examine investments, FSCO initiated legal action after having identified during a voluntary wind-up of a pension plan (unrelated to an on-site examination) that a plan administrator and an investment manager violated federal investment rules, resulting in a $1.6-million loss from inappropriate investments.

In addition, we noted that FSCO does not provide guidelines to auditors of pension plan financial statements to set out minimum expectations auditors should follow to ensure plan administrators complied with certain key requirements in the *Pension Benefits Act*. For instance, guidelines to auditors could clarify FSCO's expectations for ensuring that plan administrators exercise the care, diligence and skill in the administration and investment of the pension fund that, as per the Act, "a person of ordinary prudence would exercise in dealing with the property of another person;" the administrator is paid reasonable fees and expenses; and that plan assets were invested prudently and in accordance with federal investment rules for defined-benefit pension plans. In this way, FSCO could rely on auditors to cover key risk areas, and allow FSCO to focus its limited resources on examining other priority risk areas.

In the majority of FSCO-ordered plan wind-ups, the plan failed because the employer went bankrupt. To assess the risk that an employer is financially stable and capable of meeting its pension contribution payments, FSCO needs access to employer records and financial statements. However, the *Pension Benefits Act* limits FSCO's authority only to accessing records of the pension plan. As a result, FSCO would not know when an employer is in financial difficulty until it stops meeting its pension contribution payments, which is often when the employer is bankrupt.

Weak Monitoring of Investments of Defined-contribution Plans

While the financial risks associated with administering a defined-contribution plan are far less and significantly different than for a defined-benefit pension plan, primarily because the amount of pension liability is limited to the assets available in a defined-contribution plan, we noted that FSCO does very little to monitor whether defined-contribution pension plans are administered in accordance with the requirements of the *Pension Benefits Act* and the interests of plan members. Defined-contribution pension plan members decide how their pension contributions are to be invested by the plan administrator. The plan administrator usually offers a variety of investment options and information to educate members about each investment option. Members select investment options that best suit their investment goals. Thus, the members, rather than the plan sponsor, bear the investment risk.

As noted earlier in this report, a plan administrator of a defined-benefit pension plan must submit an annual Investment Information Summary; however, FSCO does not require such a report for defined-contribution pension plans. Plan administrators are required to report an annual information return that states only the market value of assets at the beginning and end of the reporting period and net investment income or loss. As at December 31, 2013, the market value of total assets reported on the annual information returns was $19.2 billion for 3,073 defined-contribution pension plans.

Plan administrators of defined-contribution plans are not required to report on expenses related to managing investments, administrative expenses and overall plan expenses or the asset mix of the plan. As well, no certification is required from plan administrators that all investments were made in accordance with the members' investment selections.

The notes to financial statements for defined-contribution plans contain information on types of investments in the plan. However, as noted earlier, FSCO did not follow-up with plan administrators for non-filing of financial statements, which were predominately from 800 defined-contribution pension plans. Moreover, FSCO generally did not review the financial statements of defined-contribution pension plans.

We also noted that during the 14 examinations of defined-contribution plans that FSCO conducted over the last three fiscal years, it did not assess the investments in detail or whether the plan invested the assets in accordance with options selected by members.

RECOMMENDATION 4

To ensure examinations of pension plans conducted by the Financial Services Commission of Ontario (FSCO) provide an effective level of assurance that plan administrators are operating in accordance with statutory requirements, FSCO should:

- conduct more plan examinations and select plans for examination based on risks to members of the plan;
- ensure that its procedures for examining plans effectively address the risks associated with investments managed by plan administrators;
- provide guidelines to auditors of pension plan financial statements that set out minimum expectations for ensuring compliance with key requirements of the *Pension Benefits Act* as part of these audits;
- ensure it has the necessary employer information to identify plans at risk before employers launch bankruptcy proceedings; and
- establish an examination program for defined-contribution plans that provides effective monitoring and protection to plan members.

FSCO RESPONSE

FSCO's pension examination process has been one of continuous improvement and the scope of the examinations continues to be broadened. For example, in addition to increased compliance checks, assessment of plan governance has now become a significant part of an examination.

As part of its continuous improvement for examinations, FSCO will review and consider these recommendations when it incorporates the examination process into the risk-based regulation framework in order to provide a more holistic approach for selecting plans for examinations. The review will also consider the appropriate frequency of examinations of plans and the implication on FSCO's resources. FSCO will undertake to provide advice to the government to identify if any legislative changes would be required to incorporate these recommendations.

FSCO will consider providing guidance to auditors of pension plan financial statements.

Enhanced Disclosure to Members on Plan Performance

While pension plan members receive information on their expected benefits, there is room for improvement in the information provided on their plans' performance and expenses, including information that would help members assess how their plan performed compared to other similar plans.

Pension plan administrators are required by the *Pension Benefits Act* to provide plan members with an annual pension statement that includes member-specific information on their benefits and contributions. For instance, defined-contribution pension plan administrators must disclose the total of employee and employer contributions to the member's pension, and the investment income on these funds. Defined-benefit pension plans must state the annual pension amount payable at the plan member's normal retirement date, and whether the plan is covered by the PBGF. Effective January 1, 2012, the annual statement of defined-benefit plan members must also include the most recent transfer ratio (similar to the solvency ratio) of the plan, an explanation of the transfer ratio and how it relates to the funding level of members' benefits, and, where applicable, a statement that additional payments are being made to eliminate underfunding of the plan.

While there is no requirement for plan administrators to provide an annual report and financial statements to members, some plans do so voluntarily. Upon request to either the plan administrator or FSCO, members can receive all information returns that the plan administrator provides to FSCO, such as annual financial statements, investment information returns and actuarial valuation reports.

The federal *Pension Benefits Standards Act* contains member disclosure requirements similar to Ontario's. However, the federal Office of the Superintendent of Financial Institutions provides additional disclosure guidance to pension plan administrators to ensure that members receive appropriate information on their plans. For example, OSFI recommends that administrators disclose to their members a plan's portfolio management strategies, investment performance in relation to performance goals, comparison of investment performance with relevant benchmarks, any illiquid assets held by the plan, and significant expenses incurred by the plan, with a comparison to the previous year.

Ontario's disclosure rules are such that the annual pension statement provided to members offers little information on how judiciously their plan's assets are being managed. This makes it difficult and onerous for a member to assess the performance of the plan administrator. For instance, members could find it useful to receive information on plan administrative and investment expenses, including the performance of their plan's expenses and investments compared to other similar pension plans, along with benchmark indices for the types of investments held.

As well, the *Pension Benefits Act* requires that pension plans submit annual financial statements to FSCO, but not to plan members. Financial statements, along with annual reports on the plan's performance, would help members to better evaluate the financial position of their pension plan.

In addition, plans must supply annual pension statements to active pension plan members (those still working for the employer), but not to those who are retired and collecting pensions or to former members (those who have left the employer as a result of termination or voluntary departure, but still retain entitlements under the pension plan). In May 2010, legislation was passed that amended the *Pension Benefits Act* to require plan administrators to provide former and retired members with annual statements; however, this amendment still requires proclamation by the Lieutenant Governor and no date for this has been set.

Public Reporting of Pension Plan Performance and Regulatory Oversight Could Be Enhanced

FSCO currently reports information to the public about pension plans as part of its annual report. Most of the information is statistical, such as pension plan membership, number and types of pension plans, the number of plan registrations and the number of wind-ups. FSCO also issues an annual defined-benefit funding report, which contains only summary information on the overall pension plan solvency position in Ontario. No detailed financial information on individual pension plans is reported. In our view, plan members would not find the current report useful for assessing how FSCO protects their interests and how well their plan performed and was administered in comparison to other plans and benchmarks.

FSCO does not make public its solvency watch list, even in summary form. FSCO senior management told us that because the *Pension Benefits Act* does not explicitly state that names and details of pension plans with solvency deficiencies should be reported publicly, it has not made a practice of doing so. FSCO also told us it has concerns about releasing third-party confidential information that may be subject to the *Freedom of Information and Protection of Privacy Act*. Thus, members of pension plans and the public at large would not necessarily be aware of solvency issues.

We noted in particular two other jurisdictions—the Australian Prudential Regulation Authority (APRA) and the Pensions Regulator in the United Kingdom—that provided much more information annually to the public on their regulatory activities and the management and performance of pension plans.

The Pensions Regulator releases an annual survey on the governance of pension plans with a focus on the composition and activities of the boards of trustees. APRA also releases annual details on the average composition of boards overseeing pension plans, including the average number of members on the board and percentage of female directors on the board.

APRA annually provides breakdowns on the overall assets and liabilities of pension plan categories (e.g., corporate or public sector), including what portion of assets came from investment income or gains and the amount of expenses related to administration and investing. The average rate of return and 10-year rate of return is provided for all pension plans in aggregate, as well as by pension plan category, and the actual one-, five- and 10-year rates of return are provided for each of the 200 largest pension plans on an annual basis. This reporting is similar to that required for mutual funds in Canada. For defined-contribution pension plans, both regulators provide reporting on the number of investment choices that are made available by pension plans for their members.

Both regulators publicly report on their stakeholders' perceptions of the regulator's overall performance and effectiveness based on surveys.

RECOMMENDATION 5

To ensure that pension plan members get more detailed disclosures about their pensions, and about the regulatory oversight performance of the Financial Services Commission of Ontario (FSCO), FSCO should:

- identify and seek to implement improvements to statutory annual disclosure requirements of a plan administrator that would provide more meaningful information to all members on the plan's performance and expenses, and how their plan performed compared to other similar plans and relevant benchmarks; and
- reassess its annual public reporting on pension plans in Ontario to provide more useful information for assessing how FSCO protects members' pension interests and how well their plan performed and was administered in comparison to other plans.

FSCO RESPONSE

FSCO agrees that more meaningful information to plan members on plan performance and expenses would be useful. In October 2014, the Ministry of Finance posted draft regulations for consultation with stakeholders on information to be provided to retired and former members.

FSCO will seek opportunities to provide additional information about its activities, including the findings arising from its on-site examinations, within its current resource constraints and ensure such disclosure would not violate privacy legislation requirements.

Financial Services

Weak Oversight of Co-operative Corporations that Raise Millions from Investors

The Licensing and Market Conduct Division (Division) is responsible for registering financial institutions in accordance with their respective legislations. While registration and oversight processes for credit unions, caisses populaires and loan and trust corporations were satisfactory, we concluded that FSCO had limited authority under the *Co-operative Corporations Act*, and its processes for registering and protecting investors of co-operative corporations (also referred to as co-ops) were not commensurate with the risks to investors and the significant amounts involved. As of March 31, 2014, 1,773 co-operative corporations were registered to operate in Ontario.

Co-ops are owned and controlled by their members and are incorporated under the *Co-operative Corporations Act*. Co-op members pool their resources to provide themselves with products, services, employment and housing at cost, and can sell shares to members of the general public, even though those people don't necessarily receive goods or services from the co-op. In 2009, the *Green Energy Act, 2009*, amended the *Co-operative Corporations Act* to allow for the creation of co-ops that generate and sell electricity from renewable energy sources. Renewable energy co-ops are exempt from the usual co-op requirement that they conduct at least half of their business with co-op members. Over the past two calendar years, 64 of the 116 co-ops registered by FSCO were in the renewable energy sector.

Under the *Co-operative Corporations Act*, all co-ops with more than 35 members and with plans to raise over $200,000 in funding must first file an offering statement with FSCO and get back from FSCO a statutory receipt approving the selling of shares or securities to existing or prospective members or shareholders. FSCO reviews offering statements to ensure full, true and plain disclosures are made, including risks to investors.

Over the previous three fiscal years ending March 31, 2014, FSCO issued a total of 57 receipts for offering statements filed by co-ops, totalling a maximum funding level of $371 million; 41 of these 57 offering statements allow the co-ops to raise more than $1 million, ranging from $1.2 million to $48.2 million.

We noted that FSCO has not allocated any resources to ensuring that co-ops present to potential investors only approved (receipted) offering statements by, for instance, listing all approved offering statements on their websites for the public to check. FSCO also does not conduct any ongoing monitoring of co-ops to ensure that funds are being invested in the projects outlined in the offering statements, nor does it conduct ongoing examinations of these co-ops to ensure they comply with the requirement of the *Co-operative Corporations Act*, including that FSCO approve offering statements.

In addition, FSCO does not require criminal background checks for the boards of directors or officers of new co-ops that seek to be registered, and prior to their issuing any offering statements.

We noted that FSCO's approving of offering statements replicates the similar role of the Ontario Securities Commission (OSC) for providing protection for investors under the *Securities Act*. However, under the *Co-operative Corporations Act*, investors do not have the protections that are available under the *Securities Act*, which include civil liability for directors, issuers and underwriters for misrepresentation in the prospectus; registration requirements for dealers, salespeople, underwriters or advisers selling securities of corporations; and stronger enforcement penalties. In addition, the OSC has the expertise, experience and capacity to review prospectuses filed in connection with public offerings. FSCO told us it consulted with the OSC in September 2011 to ensure the renewable energy co-ops' offering statement reviews under the *Co-operative Corporations Act* were conducted to similar standards used by the OSC for its prospectus reviews. FSCO has had to develop the expertise to review offering statements from co-ops because these reviews are entirely different from the reviews performed for the other FSCO-regulated sectors.

In accordance with the *Co-operative Corporations Act*, the Minister of Finance's Schedule of Required Fees allows FSCO to collect $50 per offering statement it reviews. We noted this fee is not commensurate with the work required by FSCO and generates total revenue of under $1,000 from the offering statement fees. In comparison, the OSC charges $3,750 for each prospectus filing review. FSCO receives a $500,000 annual allocation from the government, which subsidizes FSCO's activity in the co-op sector. Except for the early renewable energy offering statement reviews in 2010/11 when costs exceeded $1 million, the annual allocation along with the fees cover FSCO's actual costs.

RECOMMENDATION 6

To adequately protect members and investors of co-ops, the Financial Services Commission of Ontario (FSCO) should seek to have the necessary legislative authority under the *Co-operative Corporations Act* to allow it to ensure that:

- all board members have criminal checks before the co-op is registered and any offering statements are issued;
- all approved offering statements are listed on FSCO's website;
- it conduct ongoing monitoring of co-ops; and
- fees charged to co-ops to review offering statements are commensurate with FSCO costs.

In addition, FSCO should consult with the Ontario Securities Commission on the benefits of sharing or transferring the responsibility of reviewing offering statements.

FSCO RESPONSE

FSCO agrees with the Auditor General's view that members and investors of co-operative corporations should be protected. While some aspects of the recommendations could be acted upon immediately, some may require legislative amendments or further analysis. FSCO will work with the Ministry to identify and consider potential statutory amendments.

Several years ago, FSCO engaged in early exploratory staff discussions with the Ontario Securities Commission to understand the implications of potentially transferring the responsibility for reviewing co-operative offering statements. FSCO, in conjunction with the Ministry, will initiate further discussion with the OSC.

Licensing

FSCO licenses three types of insurance agents in Ontario. As of March 31, 2014, the active agents in each category were as follows:

- 40,522 life insurance agents who sell both life insurance and accident and sickness products;
- 6,716 general insurance agents who sell insurance products other than life insurance, such as auto insurance and commercial business insurance; and
- 975 insurance agents who sell individuals just accident and sickness products.

We noted that FSCO's online insurance agent licensing system did not ensure consumers were protected because it lacked key controls to ensure licences were not issued or renewed for agents that did not meet minimum requirements, including having the required errors and omissions insurance.

Weakness in the Online Licensing System for Insurance Agents

All life insurance agents are required under the *Insurance Act* to have errors and omissions insurance coverage to cover their clients who suffer financial losses as a result of negligence or fraudulent activity committed by the insurance agent. General and accident and sickness insurance agents are not required to have errors and omissions insurance coverage individually because they are sponsored by their insurance companies. The annual licensing fee is $150 and average yearly premium for errors and omissions insurance is $800. Agents apply to FSCO through an on-line licensing system. The applicant is required to report his or her errors and omissions policy number, name of the insurance provider and expiry date. Currently, the online licensing system and FSCO staff do not verify the errors and omissions insurance information.

All applicants are required to indicate whether they have any criminal convictions, regulatory complaints or have been disciplined by another financial services regulator, or if they have ever filed for bankruptcy. Applications with these circumstances are flagged for further investigation by FSCO staff to determine whether the agent is suitable to be licensed. For all new insurance agents, FSCO also conducts a criminal background check. For all non-flagged applications, the system automatically issues a licence within a day.

We noted the insurance agent licensing system had weak controls in the following areas:

- Life insurance agents who had missing or incomplete errors and omissions insurance information in the database, or who had expired policies, were still able to receive licence renewals or an initial licence. As of June 2014, over 1,700 active agents were noted in the database to have received licences even though their insurance was expired as of the issuing dates, including one agent who had entered a 2007 expiry date for the insurance policy. In all, as of August 2014, more than 9,500 active life insurance agents (23.5% of all active life insurance agents) had missing or incomplete insurance data in the database.
- According to the licensing system database, a significant number of active agents had declared they were disciplined by another financial services regulator, had declared bankruptcy or had criminal convictions. These agents' licences were renewed without their applications being investigated by FSCO staff as required, as discussed later in this report.

Licensed Insurance Agents Operating Without Required Errors and Omissions Insurance Coverage

FSCO does not verify the information in the insurance agents online licensing system database to ensure that all agents have accurately reported on whether they have errors and omissions insurance. We noted from our testing of complaints that several agents had operated for one to three years before they were identified as not having errors and omissions insurance. Instead, FSCO relies on insurance providers to notify it of any agents that have had their policies expire or cancelled. However, it is not mandatory for errors and omissions insurers to provide this information to FSCO and only some of the 150 errors and omissions insurance providers voluntarily do this. By comparison, FSCO has agreements with all errors and omissions insurance providers for the mortgage brokerage sector to notify it if a brokerage does not have insurance.

FSCO has contacted approximately 550 life insurance agents annually where insurance providers had reported to FSCO that the agents did not have errors and omissions insurance. However, we noted that it did not contact all agents who were reported to it as not having insurance. FSCO does not record the number of agents reported to it as not having insurance.

In addition, FSCO does not gather information from life insurance agents or their insurers on the number of claims filed by clients against agents and which of those claims were valid. This information would be useful for assessing the conduct of certain agents, and would also help the industry when it considers changes to the licensing process and whether regulatory changes are needed.

In contrast, FSCO requires the mortgage brokerage sector to provide this kind of information. Each brokerage must report to FSCO the errors and omissions claims against the firm and its brokers and agents that are paid by their insurance providers. Brokerages must provide brief explanations for any claims paid. In 2011, 24 brokerages received 38 errors and omissions claims, and 16 were paid out;

in 2012, 37 brokerages received 55 claims, and 11 were paid out; and in 2013, 37 brokerages received 56 claims and 10 were paid out.

RECOMMENDATION 7

In order to make its licensing system and procedures effective so that only qualified agents are given licences, the Financial Services Commission of Ontario (FSCO) should ensure that:

- its online licence system has the necessary controls to identify and reject licences for agents who do not meet minimum requirements;
- it establishes agreements with all agents' errors and omission insurance providers to provide FSCO with timely information on agents' compliance with insurance requirements, and information about consumer claims made against agents; and
- it investigates all agents who do not meet minimum standards, particularly for errors and omissions insurance requirements.

FSCO RESPONSE

FSCO welcomes the Auditor General's observations about its life insurance agent licensing system and procedures. The second phase of implementation of FSCO's Enterprise Development System will begin in July 2015 and once fully implemented, it will support complete data gathering, better internal controls, improved risk assessments and compliance, plus more market intelligence, most of which is already under way for the service provider sector. In addition, a data steward role will be created in July 2015 to manage and monitor the electronic data and establish early warning flags for inconsistent or dated information.

Life insurers are currently required to ensure that each agent complies with the *Insurance Act*, the regulations and the agent's licence. This includes ensuring that agents maintain required errors and omission insurance (E&O) coverage. FSCO will explore establishing information-sharing agreements with E&O insurers to ensure agent compliance with E&O insurance requirements, and to receive information about claims made against agents. The Superintendent will also leverage the information available from the Commercial Liability Statistical Plan for information about claims made by life insurance agents.

FSCO expects that these changes will facilitate more robust and targeted compliance activities in conjunction with its risk-based approach to regulation, as published in its Regulatory Framework.

Market Conduct

Slow Handling of Complaints

The Licensing and Market Conduct Division (Division) is responsible for dealing with complaints received by FSCO. When a complaint is received, the Division conducts an analysis and then may investigate to see whether enforcement action is needed. Over the past five fiscal years, FSCO has received an average of more than 1,100 complaints a year, about half of which were from consumers and the rest from industry stakeholders or other financial service regulators. As **Figure 11** indicates, 95% of complaints pertain to the insurance and mortgage brokerage sectors.

FSCO measures whether it closes 80% of consumer complaints within 75 calendar days and 98% of all complaints within 365 calendar days. The Division monitors the timeliness of complaint resolution and follows up on the complaints over 365 days. The majority of complaints are closed due to insufficient evidence or no findings, an average of around 20% end with a letter of warning or caution, and about 10%, or 105 complaints annually, are forwarded to its Investigations Unit. FSCO has generally met its timelines for simple complaints, but we noted that several complaints with high risks to consumers take several years to address.

Figure 11: Complaints Received by Sector, for the years ending March 31, 2010–2014[1]

Source of data: Financial Services Commission of Ontario

Regulated Sector	2010	2011	2012	2013	2014
Co-operative corporations	4	2	2	7	8
Credit unions and caisses populaires	24	22	29	35	35
Insurance[2]	614	716	965	720	730
Loan and trust	7	6	2	3	8
Mortgage brokers	354	411	351	343	319
Total	**1,003**	**1,157**	**1,349**	**1,108**	**1,100**

1. Complaints were received about both individuals and companies. FSCO did not have a breakdown of the two.
2. About 60% of these complaints pertain to the auto, property and casualty insurance sectors for the years 2013 and 2014. FSCO did not have a breakdown for the years 2010, 2011 and 2012.

We noted that several complaints handled by the Division incurred significant delays or ended in weak enforcement action. For example:

- In June 2013, a complaint was lodged against a credit union for possible conflict of interest and fiduciary breach on the part of the general manager of the credit union. There was minimal action on the file until May 2014, or 11 months later, when the complaint was transferred to another compliance officer. A warning letter for the conflict of interest was sent to the general manager of the credit union in September 2014.
- In September 2010, a complaint was received against a life insurance agent alleging client signatures were forged. The file was not forwarded to the Investigations Unit until March 2012, or 18 months later, during which time inquiries were made by the compliance officer. The final report was not completed until April 2014. In June 2014, the case was dropped by FSCO due to insufficient evidence.
- In February 2012, an anonymous complaint was received about a mortgage agent operating after having previously declared bankruptcy. The mortgage agent also had pleaded guilty to three charges under the *Bankruptcy and Trustee Act* in 2012 for failing to comply with conditions of his bankruptcy. On his 2010 and 2012 licence renewal applications, the mortgage agent did not disclose this information to FSCO as required. An investigative report was completed in April 2013. The complaint file was then transferred to legal services, and it took until March 2014, or 25 months after the complaint was filed, before FSCO issued a proposal to revoke the agent's licence. The agent requested a hearing to oppose the order, which was scheduled for October 2014.

Significant delays in handling, investigating and resolving complaint files affect both the complainants who are awaiting outcomes, as well as other consumers whom these agents or brokers continue to serve. Quickly finalizing complaint investigations may minimize the risk to complainants and other consumers.

Insufficient Proactive Examination Activity by FSCO

As **Figure 12** indicates, the Division has a program of conducting proactive onsite examinations only for mortgage brokerages; no other regulated financial institutions or insurance agents are examined unless an investigation has been initiated due to a complaint. Based on the examination activity, it would take the Division about 10 years to examine mortgage brokerages, brokers and agents, even without the other sectors being examined.

Examinations are intended to ensure compliance with key legislative requirements. For instance,

Figure 12: Examinations of Regulated Financial Sectors

Source of data: Financial Services Commission of Ontario

Regulated Financial Sector	# Licensed or Registered in 2014	Average Annual Examinations Completed Over Last Three Years	# of Years to Review the Entire Sector
Mortgage brokerages*	1,172	120	10
Life insurance agents	40,522	0	Never
General insurance agents	6,716	0	Never
Accident and Sickness Insurance Agents	975	0	Never
Credit Unions and caisses populaires	129	0	Never
Loans and trusts	52	0	Never
Co-operative corporations	1,775	0	Never

* FSCO examinations of mortgage brokerages include brokers and agents, who must work for a brokerage.

examinations of mortgage brokerages validate that the brokerage has the required errors and omissions insurance and has proper policies and procedures in place for retaining records and handling complaints. Because FSCO does not proactively examine the other regulated financial institutions and insurance agents for which it is responsible, the institutions might not be complying with requirements and that lack of compliance would go undetected.

The responsibility for overseeing and conducting inspections of insurance brokers, including those who sell home, auto and business insurance, was delegated to the Registered Insurance Brokers of Ontario (RIBO) by the Ontario government in 1981. RIBO handles complaints, licensing and examinations of its almost 18,000 brokers. In comparison to the Division's rate of examination of mortgage brokerages that would take 10 years to complete, we noted that RIBO has established a goal to examine every insurance broker at least once every five years.

The need for FSCO to conduct examinations of insurance agents was apparent from a recent product suitability review. FSCO conducted the first-time review in May 2014, to better understand the process that life insurance agents use at the point of sale, when making product recommendations to prospective policyholders. The review concluded that many sales activities are verbal, without any paper trail. FSCO also discovered that although 90% of agents stated they disclosed a conflict of interest to their clients when one existed, only 50% did so in writing as required by the *Insurance Act*.

To comply with continuing education requirements, insurance agents must report when renewing their licences that they have completed 30 hours of continuing education. To ensure agents are not giving misleading information, the Division may ask them to provide verification that the continuing education requirements were completed as reported. However, we noted that only 10 agents were audited in 2012/13, and only 50 were audited in 2013/14, out of approximately 15,000 agents who renew their licences each year.

Agents Disciplined by Other Regulatory Authorities Not Investigated Immediately

Approximately 50% of life insurance agents are members of other investment-related regulatory associations, such as the Mutual Fund Dealers Association of Canada and the Investment Industry Regulatory Organization of Canada. Licensed mortgage brokers or agents may also be licensed by the Real Estate Council of Ontario.

We reviewed the publicly reported disciplinary notices of these regulatory authorities and found a number of licensed life insurance agents and mortgage brokers and agents had been formally disciplined by them. For instance, as of June 2014, the Mutual Fund Dealers Associations of Canada had disciplined 66 members who were also active licensed life insurance agents, and some of these agents were permanently prohibited from further selling of mutual funds.

We sampled the Division's records to determine whether it had launched its own examination into the business practices of agents who had been disciplined by other regulatory authorities to ensure similar wrongdoings were not occurring in the FSCO-regulated sectors. We found the Division did not have adequate procedures or information-sharing arrangements with these other associations to be notified immediately when disciplinary actions occurred, and it did not routinely initiate any proactive examination of disciplined life insurance agents when it was aware of them. Instead, when it became aware of a disciplinary action by another regulator, the Division flagged the agent's file. No further action is taken until the licensee applies for his or her licence renewal, at which time the Division may investigate the licensee's suitability. As a result, licensed agents with serious regulatory disciplinary action against them by another regulator are allowed to operate for years without being further investigated in a timely manner by FSCO, which puts consumers at risk.

Following are examples of cases where we felt that more proactive and timely action from the Division would have been prudent to protect consumers:

- A life insurance agent was permanently banned and fined $350,000 in March 2009 by the Investment Industry Regulatory Organization of Canada for having undisclosed financial interests and dealings in accounts of two of his clients, including misappropriating nearly $500,000 from a client's account. The Division was unaware of this disciplinary action. In July 2010, the agent did not report the conviction on his licence renewal application, and the Division renewed the agent's licence. FSCO became aware of the discipline action in August 2010, over 17 months after the disciplinary action had occurred. FSCO then launched an investigation based solely on the agent's suitability and in April 2012, FSCO finalized its investigation and revoked the agent's licence. In the end, the life insurance agent operated under a FSCO licence for three years after the disciplinary action by another regulatory body.
- Another life insurance agent was permanently banned by the Mutual Fund Dealers Association of Canada and fined $40,000 in May 2012 for selling unapproved securities to his clients, resulting in their incurring substantial losses. The Division was notified in June 2012, but did not launch an investigation until December 2013—19 months later—when the agent applied for a licence renewal. We noted that the agent's licence was renewed in March 2014 because the investigation had not yet concluded and there had not been enough evidence gathered to deny the renewal at that time.
- A mortgage broker renewed his licence using FSCO's online licensing system in 2008 and 2010. On the 2010 application, the broker disclosed that he had failed to report on his 2008 application that he had several regulatory sanctions and convictions, including failing to disclose and remit retail sales tax of $76,000 in 2008; and that he had had his registration as a motor vehicle salesperson revoked in 2007, and his real estate broker licence revoked in 2010. Despite an ongoing investigation by the Division since 2010, the broker's licence was renewed in 2010, 2012 and 2014. In October 2014, seven years after the disciplinary action by another regulatory body, a final decision was made to revoke the agent's licence.

We also found FSCO's enforcement actions against licensed life insurance agents did not mirror the actions taken by other financial services regulators. Several agents who had received multi-year suspensions or prohibition bans from the Mutual

Fund Dealers Association of Canada only received from FSCO letters of caution warning them that regulatory action may be taken in the event of another violation.

RECOMMENDATION 8

In order to ensure that the Financial Services Commission of Ontario (FSCO) meets its mandate to provide regulatory services that protect the public interest and enhance public confidence in the regulated financial sectors, FSCO should:

- take timely action to investigate complaints, and have adequate systems and procedures in place to monitor the timelines and outcomes of its handling of complaints and investigations;
- assess the need for proactive investigations in each of its regulated financial sectors that would allow for periodic examinations of all registrants and licensees;
- identify common issues from its examination activities and share them with the industry, and consider action that can be taken to mitigate their causes; and
- establish systems and procedures to promptly identify, investigate and determine the continued suitability of registrants and licensees who have received sanctions from other associations.

FSCO RESPONSE

Since September 2013, FSCO has consistently exceeded its complaint closing rate standards, which are among the highest standards for those regulators that have such performance measures. Processes are now in place to monitor timelines and outcomes of complaints and investigations.

FSCO agrees that proactive compliance is an important part of a robust monitoring and compliance framework that protects the public interest and enhances confidence in the regulated sectors. FSCO's Regulatory Framework focuses on bringing licensees into compliance through a multi-faceted approach. FSCO will assess the need for conducting periodic proactive investigations, as well as other factors that may cause FSCO to initiate an examination, in each of its regulated financial sectors as part of its ongoing risk-based regulation framework.

FSCO commits to providing more timely publication of reports for the industry identifying common issues from its examinations.

FSCO will explore further information-sharing arrangements to ensure that licensees sanctioned by other regulators are assessed more quickly, in accordance with governing legislation and with the due process to which they are entitled. For example, and more recently, FSCO has negotiated a memorandum of understanding with the Mutual Fund Dealers Association. Any enforcement action taken by FSCO, if warranted, will be based on those penalties authorized under the applicable laws.

Potential Benefits to Transferring Regulatory Oversight to Associations or Other Government Regulators

FSCO is required by the *Insurance Act* and the *Mortgage Brokerages, Lenders and Administrators Act, 2006*, to issue licences and review market conduct for mortgage brokerages, mortgage brokers, mortgage agents and insurance agents. FSCO is responsible for directly overseeing more than 55,000 registrants and licensees in the insurance sector (this does not include insurance brokers, who are licensed by the Registered Insurance Brokers of Ontario) and more than 11,000 in the mortgage sector. We felt that these large numbers could justify the industries assuming greater responsibility for overseeing their professions, including their establishing self-regulation and consumer protection funds, as is the case in many other similar self-regulated service industries. **Figure 13** highlights some of the more recognizable self-regulating entities.

If responsibility for oversight of regulated financial sectors were to fall to associations that oversaw industries, FSCO could assume the role of overseeing those associations rather than overseeing individual companies. This would require that FSCO recommend changes to the legislation that governs these professions, but it would allow FSCO to focus its resources on more serious and strategic matters pertaining to the regulated industries.

FSCO currently relies on delegated regulatory oversight by two associations:

- As mentioned earlier, the Registered Insurance Brokers of Ontario (RIBO) regulates the almost 18,000 insurance brokers in Ontario, in accordance with the authority granted to it under the *Registered Insurance Brokers Act*. It is self funded and maintains a Professional Indemnification Fund that covers losses on claims of premiums misappropriated by brokers. On-site examinations are conducted regularly to evaluate brokers' practices and to verify information reported during the licensing application and renewal process. RIBO is required to maintain both a Complaints Committee and a Discipline Committee. RIBO conducts investigations of brokers based on complaints from the public and issues arising from the spot checks. FSCO conducts an annual examination of the affairs of the Registered Insurance Brokers of Ontario to ensure it is meeting the legislative requirements.
- The Ontario Mutual Insurance Association examines all 42 farm mutual insurance firms under an agreement with FSCO. Under the *Insurance Act*, a Fire Mutual Guarantee Fund was established to wind up farm mutual

Figure 13: Examples of Self-Regulating Professional Organizations in Ontario

Prepared by the Office of the Auditor General of Ontario

Profession	Name of Regulating Entity	Issues Licences to Members	Responsible for Setting Members' Standards and Professional Development Requirements	Administers a Consumer Protection Fund to Cover Losses Caused by its Members	Responsible for Disciplinary Action Against Members
Accountants and auditors	Chartered Professional Accountants of Ontario and Public Accountants Council for the Province of Ontario	Yes	Yes	No	Yes
Funeral directors	Board of Funeral Services	Yes	No	Yes	Yes
Insurance brokers	Registered Insurance Brokers of Ontario	Yes	Yes	Yes	Yes
Investment dealers	Investment Industry Regulatory Organization of Canada	Yes	Yes	Yes	Yes
Lawyers and paralegals	Law Society of Upper Canada	Yes	Yes	Yes	Yes
Motor vehicle salespeople	Ontario Motor Vehicle Industry Council	Yes	No	Yes	Yes
Mutual fund dealers	Mutual Fund Dealers Association of Canada	Yes	No	No	Yes
Real estate and business brokers	Real Estate Council of Ontario	Yes	Yes	Yes	Yes
Travel sales	Travel Industry Council of Ontario	Yes	No	Yes	Yes

insurance companies that ran into financial difficulties. The Association monitors insurers' solvency and administers the fund, which has never been used.

FSCO also regulates financial sectors with only a few registrants when other government regulators could assume this responsibility. For example, FSCO directly regulated only 18 of 339 insurance companies operating in Ontario; 279 insurers are regulated by the federal Office of the Superintendent of Financial Institutions (OSFI) since they are federally incorporated; and 42 farm mutual insurance firms are examined by the Ontario Mutual Insurance Association, with FSCO oversight of the Association. It is inefficient for FSCO to oversee such a small number of companies, and it would likely be more practical to establish arrangements with OSFI to oversee all insurers.

Similarly, the number of credit unions and caisses populaires FSCO oversees has declined from 251 in 2004 to 129 in 2014.The federal government enacted changes in December 2012 that allow credit unions to incorporate federally, instead of provincially as previously required, and to be governed by the federal *Bank Act*, which would transfer regulatory oversight to the OSFI.

RECOMMENDATION 9

To ensure that regulatory processes exist commensurate with the size and maturity of the industries, the Financial Services Commission of Ontario (FSCO) should explore opportunities to transfer more responsibility for protecting the public interest and enhancing public confidence to new or established self-governing industry associations, with oversight by FSCO. Areas that could be transferred include licensing and registration, qualifications and continuing education, complaint handling and disciplinary activities. In addition, associations could be responsible for establishing industry-sponsored consumer protection funds to provide more confidence in their services by the public. FSCO should then submit such proposals to the Ministry of Finance for consideration of legislative changes that would make it possible.

For regulated financial sectors, including insurance companies, credit unions and caisses populaires that have fewer registrants, FSCO, in conjunction with the Ministry of Finance, should explore the possibility of transferring its regulatory responsibilities to the federal Office of the Superintendent of Financial Institutions.

FSCO RESPONSE

It should be noted that the responsibility for initiating legislative reviews of regulatory requirements for each financial sector rests with the government.

Modern financial services regulation calls for a holistic view of the financial services rather than a siloed approach. While there are many reasons to create self-regulatory agencies, most self-regulatory organizations were created to oversee a single sector. As a regulator of many financial services, FSCO looks at the complex profile of the individual or business in the context of today's highly inter-connected financial services marketplace and not just as a licensee in a single sector. FSCO will support the Ministry of Finance when legislative changes are being considered.

With respect to transferring some regulatory responsibilities to another regulator, the government announced in the 2013 Budget that Ontario will be phasing out responsibility for insurance company solvency supervision. FSCO is responsible for market conduct of the credit unions and caisses populaires sector whereas the Deposit Insurance Corporation of Ontario is responsible for solvency regulation of the sector. The role of the two regulators for oversight of the credit union sector will be examined by the government as part of the five-year review of the *Credit Unions and Caisses Populaires Act, 1994* which commenced on October 1, 2014.

Appendix—Pension Plan Membership, for the years ending March 31, 2011–2013

Source of data: Financial Services Commission of Ontario

	2011	2012	2013
Single-employer pension plans/Number of Plans	**7,646**	**7,646**	**7,396**
Defined-benefit pension plans	**4,402**	**4,419**	**4,241**
Active members	667,000	661,000	684,000
Retired members, deferred members and other beneficiaries	621,000	622,000	659,000
Total members	**1,288,000**	**1,283,000**	**1,343,000**
Defined-contribution pension plans	**3,244**	**3,227**	**3,155**
Active members	340,000	343,000	345,000
Retired members, deferred members and other beneficiaries	55,000	56,000	58,000
Total members	**395,000**	**399,000**	**403,000**
Total Members (single-employer pension plans)	**1,683,000**	**1,682,000**	**1,746,000**
Multi-employer pension plans/Number of plans	**121**	**118**	**118**
Defined-benefit pension plans	**82**	**77**	**77**
Active members	375,000	365,000	367,000
Retired members, deferred members and other beneficiaries	453,000	457,000	469,000
Total members	**828,000**	**822,000**	**836,000**
Defined-contribution pension plans	**39**	**41**	**41**
Active members	31,000	32,000	38,000
Retired members, deferred members and other beneficiaries	20,000	24,000	24,000
Total members	**51,000**	**56,000**	**62,000**
Total Members (multi-employer pension plans)	**879,000**	**878,000**	**898,000**
Jointly sponsored pension plans/Number of Plans	**7**	**11**	**10**
Defined-benefit pension plans	**7**	**11**	**10**
Active members	706,000	732,000	701,000
Retired members, deferred members and other beneficiaries	501,000	523,000	498,000
Total members	**1,207,000**	**1,255,000**	**1,199,000**
Total Members (jointly sponsored pension plans)	**1,207,000**	**1,255,000**	**1,199,000**
All pension plans/Number of plans	**7,774**	**7,775**	**7,524**
Defined-benefit pension plans	**4,491**	**4,507**	**4,328**
Active members	1,748,000	1,758,000	1,752,000
Retired members, deferred members and other beneficiaries	1,575,000	1,602,000	1,626,000
Total members	**3,323,000**	**3,360,000**	**3,378,000**
Defined-contribution pension plans	3,283	3,268	3,196
Active members	371,000	375,000	383,000
Retired members, deferred members and other beneficiaries	75,000	80,000	82,000
Total members	**446,000**	**455,000**	**465,000**
Total Members — all pension plans	**3,769,000**	**3,815,000**	**3,843,000**