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Note: This policy was originally published as Compliance Assistance Guideline #3. Due to legislative changes all references to the PBA, 1987 and Regulation 708/87 should be read as references to the PBA, R.S.O. 1990 and Regulation 909:

PBA, 1987

ss. 23(1), (2) & (4)

ss. 30(1)

s. 63

ss. 99(1)

PBA, R.S.O. 1990

ss. 22(1), (2) & (4)

ss. 29(1)

s. 62

ss. 98(1)

A Guide to Preparing, Reviewing and Amending a Statement of Investment Policies and Goals (SIP&G)

Filing Highlights

Most pension plans registered in Ontario are required to file a SIP&G. Administrators of pension plans varying in size from a few to many thousands of members must conduct an assessment and analysis of their plan's liabilities and devise appropriate policies and investment strategies for their fund assets.

This guide has been designed to assist Administrators in preparing and amending their SIP&G. The statutory minimum requirements are described: the Administrator is encouraged, however, to include any other relevant policies or factors.

Although the same statutory requirements apply to all pension plans regardless of their size, the guidelines are mainly directed to small and medium-sized pension plans that are less likely to draw on the services of professional advisers.

Guidelines

The guidelines will familiarize Administrators with the salient points of the legislation. They are not a substitute for the Regulation. For specific legal requirements, readers are directed to the *Pension Benefits Act, 1987* (the "PBA") and

Regulation 708/87, as amended.

Our principal concern is to help Administrators complete the SIP&G and the companion document, the Investment Policy Return ("IPR").

What pension plans must file a Statement of Investment Policies and Goals?

All pension plans registered with the PCO must file a SIP&G except pension plans completely invested in fully insured contracts and/or deposit administration general funds contracts regulated by the *Insurance Act*, the *Canadian and British Insurance Companies Act* (Canada), or similar provincial or territorial laws.

Although a pension plan may be exempt from filing a SIP&G, the Administrator is required to complete and certify the applicable part of the IPR and file it with the PCO. In the case of plans that were established before and were in effect on January 1st, 1988, the SIP&G is overdue and should be filed immediately.

For a pension plan currently operating under a collective agreement (subject to the *Labour Relations Act*) that was in effect on January 1st, 1988 and expires after January 1st, 1990, the Administrator must file the SIP&G and IPR 90 days after the policies and goals are adopted or by January 1st, 1991, whichever is earlier.

When a new pension plan is established, the SIP&G is required to be submitted to the Superintendent for registration of the pension plan - unless the pension plan is completely invested in fully insured contracts and/or deposit administration general funds contracts. In this case, the Administrator is required to complete and certify only the applicable part of the IPR. This application must be made within 60 days after the date on which the plan is established.

If an exempt pension plan loses its exempt status owing to a broadening of investments outside fully insured contracts and/or deposit administration general funds contracts, the Administrator is required to complete and file a full SIP&G and IPR. The Administrator is required to file within 90 days of the amendment which alters the pension plan's exempt status.

Failure to file the SIP&G and IPR by the required deadline is an offence under the PBA, 1987. As a result, any investment made after the filing deadline will be in contravention of section 63 of the PBA, 1987.

The Investment Policy Return

The IPR is an administrative form that must be completed, certified and filed together with the SIP&G. As each statutory requirement is addressed in the SIP&G, the appropriate box on the IPR should be checked off.

For the SIP&G to be acceptable for filing, the Administrator must also file an IPR. This companion document to the SIP&G derives its authority from subsection 99(1) of the PBA, 1987.

Reviewing And Amending A Previously Filed Statement Of Investment Policies and Goals

The Administrator must reconsider the investment policy and either confirm or alter it at least annually, in light of changing plan priorities. All amendments and confirmations must be filed within 90 days of the confirmation and amendment.

Policy Background

The PBA, 1987 represents a significant departure in investment policy and regulatory requirements from the previous Act. The former "legal for life" approach to investment was perceived as too restrictive and not conducive to modern

portfolio management. Through consultation with plan sponsors and the investment industry, more efficient investment policies and rules have been adopted and incorporated into the new legislation. This allows for an expanded range of investment instruments and vehicles for more flexible investment of pension assets. Relaxation of the investment rules, however, has been balanced by new requirements for prudence and greater disclosure to members.

The concept of prudence in the PBA, 1987 provides that the Administrator "shall exercise the care, diligence and skill in the administration and investment of the pension fund that a person of ordinary prudence would exercise in dealing with the property of another person". Furthermore, subsections 23(1) and (2) of the PBA, 1987 require that "The administrator of a pension plan shall use in the administration of the pension plan and in the administration and investment of the pension fund all relevant knowledge and skill that the administrator possesses or, by reason of his or her profession, business or calling, ought to possess".

This responsibility extends to decisions of the Administrator's agents, including the investment manager, custodian, professional adviser or anyone else involved in the administration of the plan. Moreover, section 63 of the PBA, 1987 expressly requires that "Every person engaged in selecting an investment to be made with the assets of a pension fund shall ensure that the investment is selected in accordance with the criteria set out in the Act and prescribed by the regulations".

The adoption of a clear investment philosophy is as important in the context of defined contribution plans as it is in the context of defined benefit plans. Whether or not the plan provides that plan members direct their contributions to particular funds and investments, the Administrator has an obligation to monitor carefully fund performance and report results to members.

The smaller plans whose funds are invested in pooled or segregated funds offered by financial institutions require separate mention. These smaller plans must still address the needs of the membership in the selection of investment vehicles. The guidelines attempt to facilitate the preparation of the SIP&G for such plans.

The new rules also increase the degree of disclosure required to be made to plan members respecting all areas of the administration of their pension plan. This includes access to the SIP&G, any amendment to it, and receipt of the financial reports of the fund. The SIP&G provides a means for Administrators and plan members to measure and monitor performance against stated expectations.

Does the PCO Approve the Investment Policy?

The PCO will not offer an opinion on the appropriateness of any investment policy for a particular pension plan; nevertheless, applicable restrictions and limitations as set out in the Regulation must be met.

Minimum Statutory Filing Requirements

The minimum requirements for the SIP&G are prescribed in the Regulation. The SIP&G must detail the plan's policies on at least the following items:

!	type of pension plan	Reg. 63(3)
!	nature of plan liabilities	Reg. 63(3)
!	rate-of-return expectations	Reg. 63(3)(b)
!	asset mix policy	Reg. 63(3)(b)
!	portfolio diversification	Reg. 63(3)(a)
!	allowable investments and loans	Reg. 63(3)(c)
!	valuing not regularly-traded assets	Reg. 63(3)(h)
!	conflict-of-interest policy	Reg. 63(3)(d)

!	conflict-of-interest disclosure	Reg. 63(3)(e)
!	securities or cash lending	Reg. 63(3)(f)
!	retention/delegation of voting rights	Reg. 63(3)(g)

Type of Plan Reg. 63(3)

The Administrator must describe in the SIP&G the type of plan - defined benefit, defined contribution or multi-employer pension plan and the nature of the benefit, for example, flat benefit or career average benefit. The description must include the extent of employee contributions that are required by the plan, and the extent to which optional employer contributions may be made.

Plan Liabilities Reg. 63(3)

Administrators of defined benefit plans must state the nature of the plan's underlying liabilities. A detailed analysis of these liabilities is not required. There should be a brief description of the nature of the liabilities and the major factors affecting them, e.g. indexing, distribution among actives, deferreds and retirees, work force mobility, and average age of the work force. Furthermore, there should be a brief description relating the investment policy to the above factors and the projected cash flow needs under the plan. Administrators of defined contribution plans should state what minimum interest rate is paid on contributions, and the extent of their liabilities, such as a guarantee of principal.

Rate of Return Expectations Reg. 63(3)(b)

The rate of return, which will derive from plan liabilities and affect asset mix policy, should meaningfully express and quantify expected investment performance. This can be expressed in such terms as a nominal rate of return for the fund or as a real rate of return (a rate of return taking inflation into account). The rate of return should be consistent with the investment policy adopted, for example:

- ! 5% nominal rate of return;
- ! 3% real rate of return;
- ! 1% plus the increase in the TSE 300 index; and
- ! 2% plus the 9-day T-bill rate.

Administrators may also want to set out performance targets for the various asset groups of the fund, either in relation to relevant indices or to a relevant sample from a performance measurement service.

Asset Mix Policy Reg. 63(3)(b)

The asset mix policy will state the proposed diversification of the plan's assets between major asset groups, for example: Equities, 60%; Fixed Income Securities, 30%; Cash, 10%.

The Administrator should list all major factors that affect asset mix policy and relate these to the policy adopted. Among such factors may be:

- ! policy on asset-liability matching;
- ! risk tolerance levels;
- ! plan sponsor's financial strength;
- ! funded status of the plan; and
- ! expected long-term capital market trends.

Are Ranges Acceptable for the Asset Mix Policy?

Yes. The Administrator must, however, identify meaningful ranges for the percentage of the fund that the plan will devote to each asset class. The Administrator or investment manager must operate within these expressed ranges. A contemplated change in asset mix ranges or policy requires an amendment to the SIP&G, to be filed with the PCO within 90 days of its adoption.

What About Member-Directed Investments In Defined Contribution Arrangements?

In this instance, the Administrator is not responsible for establishing an asset mix policy. However, the Administrator is required to describe the members' degree of discretion to allocate investments and select available options, for example: fixed-term deposits and specified pooled funds.

Portfolio Diversification Reg. 63(3)(a)

The SIP&G must indicate the intended degree of diversification and include the limits on aggregate and individual investments. Hence, in addition to diversification across broad asset classes specified in the asset mix policy guideline, diversification within classes, and within categories and sub-categories of investments, must be specified. The SIP&G may require, for instance, a policy of diversification of bonds by different terms to maturity, or by the issuer's credit rating. This bond policy may limit the portion of the fund to be invested in corporate bonds and set a minimum to be invested in government securities. The diversification policy of the equity components might stipulate a range for the number or weighting of equity securities held. This equity policy might distinguish these securities by type or by market sector, and relate their fund representation to index weightings.

What Are The Minimum Diversification Requirements Of The Regulation?

No more than 10% of the assets - based on book value measured at the time of the transaction - can be loaned to or invested in the securities of any one person, partnership or association. For the purpose of this rule, affiliates of companies not traded publicly are treated as one company.

Investments in deposits with a bank, loan or trust corporation, credit union or caisse populaire are exempt from this 10% limit if the deposits are fully insured by the Canada Deposit Insurance Corporation, the Quebec Deposit Insurance Board or the Ontario Share and Deposit Insurance Corporation. Other exemptions also exist; for instance, the limit does not apply to investments in segregated, mutual or pooled funds that comply with the requirements set out in the Regulation. No do the restrictions limit investment in issues, bonds or debentures that are issued or guaranteed by the Government of Canada or a province or territory.

Categories And Sub-Categories Of Investments And Loans Reg. 63(3)(c)

For the purpose of the SIP&G, Administrators are required to identify the categories and sub-categories of current and intended investments and loans. These are set out in subsection 72(12)2-17 in the Regulation. Administrators and investment managers considering the inclusion of instruments not expressly included in items 2-16 should identify and describe them and their intended use under item 17. Such instruments could consist of derivative securities, limited partnerships, commodity funds, tangible assets, hybrid securities, or new investment securities and vehicles that may be created from time to time. Any use of these investments shall be made within the framework of the asset mix policy as it related to the investment policy of the fund, and shall be consistent with the concept of prudence in the context of the overall portfolio.

Valuation Of Investments Not Regularly Traded Reg. 63(3)(b)

For each major asset group, the Regulation requires the identification of the persons engaged in - and the description of the basis for - valuing investments that are not regularly traded. The policy must state, for instance, the valuation basis for real estate. Administrators are encouraged to obtain a qualified and independent appraiser's evaluation of major real estate holdings once every three years.

Conflicts Of Interest Reg. 63(3)(d) and (e)

The PBA, 1987 prohibits the Administrator's personal interests from conflicting with the exercise of duties and powers. This extends to the agents of the Administrator, including an investment manager as well as members of a pension committee or board of trustees that acts as an Administrator (subsection 23(4) of the PBA, 1987).

Some transactions involving possible conflicts of interest are either expressly prohibited in the Regulation, or may be exempted under certain conditions; the reader should examine sections 45, 65, 69 and 71 of the Regulation for descriptions of such transactions or conditions.

The Administrator should identify, in the context of a particular plan, both possible and perceived conflicts of interest that might arise from the administration of the plan and investment management of actual or proposed investments.

In addition, the SIP&G must set out the disclosure policy for conflicts of interest as described in clause 63(3)(e) of the Regulation. It will include the timing of such disclosure, to whom disclosure is to be made, and the method for removing persons in conflict from the decision-making process, where applicable. These items comprise the mechanism for dealing with conflict of interest.

Lending Of Cash Or Securities Reg. 63(3)(f)

If the Administrator plans to engage in securities lending, the SIP&G should stipulate the circumstances in which the activity will be carried out. Although the description of the circumstances may be quite general, those institutions with whom the Administrator intends to deal should be listed together with the standard terms and conditions of the contracts, and the requirements for collateral. The specific collateral requirements are set out in section 73 of the Regulation; the Administrator may opt for an even more stringent lending policy.

The lending of cash is also contemplated and guidelines on eligible loans and investments may be found in subsection 69(2) and section 70 of the Regulation. Should the Administrator want to engage in cash lending, the SIP&G should generally describe the circumstances and identify the borrower or mortgagee, and - in the same manner as for securities - state lending terms and conditions along with the requirements for collateral. The policy on lending of cash will be developed and carried out so as not to contravene the plan's policy on conflict of interest. Specific prohibitions are listed in subsection 69(1) of the Regulation.

Retention Or Delegation Of Voting Rights Reg. 63(3)(g)

The SIP&G should set out the plan's policy on voting of securities carrying voting rights - specifically, whether the Administrator will retain voting rights acquired through the plan's investments, or, if they are to be delegated, to whom. If the pension plan has a policy or policies on voting, these should be stated. The SIP&G should also describe what procedure is followed to review proxy statements and solicitations in deciding how to vote securities.

In the case of a pooled fund to which contributions are directed by members, the SIP&G should address the voting arrangements with respect to the fund.

Simplified SIP&Gs For Pooled Funds

Pension plans completely invested in pooled, mutual or segregated funds ("pooled funds") are required to file an IPR and SIP&G.

In order to streamline procedures for these plans, the PCO proposes a simplified SIP&G. The PCO has instituted a central registry for pooled fund prospectuses, offering documents, and other descriptive documents prepared by the vendors of such pooled funds.

Where the Administrator is satisfied that the pooled fund complies with the investment Regulation, and the filed documents meet the minimum statutory requirements as to the SIP&G where applicable, the Administrator may file a simplified SIP&G addressing only the following items:

- 1) type of pension plan;
- 2) nature of plan liabilities if defined benefit;
- 3) a reference to the pooled fund or funds in which the pension plan is or will be invested;
- 4) a description of asset allocation if more than one fund is selected; and
- 5) the conflict-of-interest policy regarding the selection of pooled funds.

These same requirements apply where the pension plan is invested in a combination of fully insured contracts, deposit administration general funds contracts, and pooled funds.

Plan Members' Disclosure Rights

Plan members are entitled to review the pension plan's SIP&G once annually. In addition to members, those who may inspect the document include former members, spouses (or their agents) or representatives of a trade union. The Administrator will make the information available within 30 days of receiving a written request from any of the above parties (subsection 30(1) of the PBA, 1987).

Plan members and other eligible persons may inspect plan documents at the PCO at any time during regular Commission hours, with prior notice. However, plan members are encouraged to direct their enquiry first to the Administrator of their pension plan who is obliged under the PBA, 1987 to provide the information requested.) Alternatively, members may also obtain copies of the document from the PCO upon payment of prescribed fees.

In Summary

Responsibility for completing and filing the SIP&G and IPR, and ensuring adherence to the policies by the agent, rests with the Administrator. This process provides the Administrator with an opportunity to analyze and assess the pension plan's requirements, and devise investment policies and strategy to satisfy and meet those needs.