

Is Your Default Investment Option Appropriate for Your Employees?

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Choosing a default investment option for employees is not easy. Employers who make an inappropriate choice could be liable for damages. The Office of the Superintendent of Financial Institutions ("OSFI") recently issued a [Guidance Note, providing assistance in this regard](#). The Guidance Note provides OSFI's interpretation and expectations relating to the requirements for the investment option selected by the administrator of a member choice account plan as the default investment option.

The federal pension benefits standards legislation imposes a statutory standard of care on pension plan administrators. Oftentimes, for single-employer pension plans, the employer is the plan administrator. This includes investing the assets of the pension fund in a manner that a reasonable and prudent person in respect of a portfolio of investments of a pension fund (the "Prudent Person Rule"). This also includes the plan administrator being required to use all relevant knowledge and skill that the administrator possesses or, by reason of that administrator's profession, business or calling, ought to possess.

For defined contribution accounts or additional voluntary contribution accounts in a defined benefit plan, the legislation provides that a pension plan may permit members to make investment choices among investment options offered by the plan administrator, and sets out rules related to the investment options. If a member does not make an investment choice from among the investment options offered by the plan administrator, the investment option selected by the plan administrator as the default investment option will apply.

The Guidance Note indicates that the plan administrator must select a default investment option in accordance with the Prudent Person Rule. The Guidance Note's guidance and OSFI's views include the following.

1. **Selecting a suitable default investment option.** A plan administrator can offer the same default investment option for all plan members or the default investment option could be structured to provide different investments for different members or class members. When selecting a default option, a plan administrator should take into consideration the age and/or risk profile of the plan membership, the general suitability of the default investment option as a vehicle for retirement savings purposes, and the costs associated with the investment options.

OSFI points out that two possible types of investment funds that a plan administrator could consider when selecting an investment option include: a balanced fund or a target date fund.

2. **Documenting the selection of the default investment option.** The plan administrator has a fiduciary responsibility to ensure that the pension fund's assets are invested in a prudent manner. An administrator should establish, implement and adhere to policies and procedures that support its responsibilities. In addition, the process and the rationale for selecting the default investment fund should be documented.
3. **Communicating the default investment option.** Plan administrators should pay particular attention to how the default investment option is described in plan member

communications. The description of the default investment option and its investment strategy should include: its investment objective; the type of investment and the degree of risk associated with it; its top 10 holdings by market value; its performance history; a statement that its past performance is not necessarily an indication of its future performance; the name and a description of the benchmark that best reflects the composition of the investment option; the cost associated with the investment option, expressed as a percentage or a fixed amount; and, its target asset allocation. If the default investment option is a target date fund, OSFI expects the provision of an explanation of the target date fund and an illustration of the glide path.

4. **Reviewing the default investment option.** The design, performance and continued suitability of the default investment option should be reviewed by the plan administrator on an ongoing basis. A review is especially important when certain events occur that could reasonably be expected to have an impact on the appropriateness of the default investment option, such as a change in the age and risk profile of the plan membership and significant changes in financial markets or the economy.

Comment

Although this Guidance Note technically applies to federally-regulated pension plans and members, OSFI's guidance will be helpful for plan administrators of provincially-regulated pension plans with respect to default investment options. In addition, other non-registered pension retirement savings plans where a default investment option is chosen by the plan administrator may also find this Guidance Note to be of interest. We recommend undertaking a review of this Guidance Note and taking any appropriate action for your particular circumstances.

Any member of our Pensions and Benefits Group would be pleased to advise your organization further with respect to default investment options and any other aspects of your retirement savings plan.

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