Office of the Superintendent of Financial Institutions Canada
Bureau du surintendant des institutions financières Canada

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InfoPensions

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InfoPensions - Issue 3 – May 2010

InfoPensions is the Office of the Superintendent of Financial Institutions' (OSFI's) electronic newsletter on pension issues. *InfoPensions* includes announcements and reminders on issues relevant to federally regulated private pension plans as well as descriptions of how OSFI applies selected provisions of the *Pension Benefits Standards Act, 1985* (PBSA), its regulations and directives and other OSFI guidance. Plan administrators should obtain appropriate legal and actuarial advice on how the legislation and guidelines affect their particular pension plan.

InfoPensions and PBSA Update (OSFI's predecessor pension newsletter) are available on the Pensions Page of the OSFI Web site. To automatically receive new issues of this newsletter by e-mail, subscribe through the Subscription Centre Link.

The next issue of *InfoPensions* will be posted in November 2010.

Finance Canada Legislative Process

As mentioned in InfoPensions – Issue 2, proposed changes to the federal private pension legislative framework were announced on October 27th, 2009 and details are included in a *Backgrounder* document available on Finance Canada Web site. Some of these proposed changes have been included as part of the Budget Implementation Act (Bill C-9) introduced on March 29, 2010[1]. Others have been included as a first round of amendments to the Pension Benefits Standards Regulations, 1985 (PBSR) released by Finance Canada on May 3, 2010 for public comment.

On May 18, 2010, OSFI posted proposed changes to Section 2 of the *Directives of the Superintendent* issued on June 30, 1987. The proposed changes set out the frequency requirements for the preparation of actuarial reports referred to in subsection 12(3) of the PBSA and are made in conjunction with the PBSR amendments.

These proposed legislative and regulatory amendments include measures to:

Enhance Protection to Members

- Full funding on plan termination
- Immediate vesting
- Enhanced disclosure to members and retirees
- Introduce void amendments that reduce the solvency ratio if the resulting ratio will be less than 0.85
- Eliminate employer declared partial terminations

[1] Part 9 of Bill C-9 outlines the proposed PBSA amendments

See Legislative Process on Page 2

Canada

Finance Canada Legislative Process (cont'd)

Reduce Funding Volatility

- Base solvency funding on average solvency ratios, rather than point-in-time solvency deficiencies
- Allow Letters of Credit (LOCs) in lieu of solvency special payments (up to 15% of plan assets)

Modernize Investment Rules

- Eliminate quantitative limits on Canadian resource properties and real estate

Others

- Resolution of plan-specific funding problems
- Allow Life Income Fund (LIF) style payments from DC plans

The timing of the PBSR amendments announced on May 3rd is not dependent on the passage of the PBSA amendments in the Budget Implementation Act. Once the timing of the new Regulations is established, OSFI will consider an appropriate deadline for this year, taking into account the time needed for plan sponsors to consider their options and make appropriate decisions. As soon as practicable, OSFI will announce the deadline by which actuarial reports must be filed.

Required Filings for Terminated Plans

When a pension plan has terminated and the administrator has been informed that the Superintendent has approved the termination report, OSFI requires a plan administrator to continue to file annual financial statements while there are any assets remaining in the pension fund.

Plan administrators must notify OSFI in writing when all assets have been distributed and submit a year-to-date financial statement from the custodian. We would also like to remind administrators that all documents filed with OSFI should include the plan's five digit *PBSA* registration number.

Unlocking – Small Benefits

OSFI has recently received questions regarding paragraph 18(2)(c) of the *PBSA* and the unlocking of small benefits. We would like to remind plan administrators that if a plan permits, a pension benefit may be unlocked when:

- a member ceases membership; and
- the amount of the annual pension that would be payable at the member's pensionable age is less than 4% of the Year's Maximum Pensionable Earnings (YMPE) in the calendar year in which the member ceases participation in the plan.

Any increase in the member's pension benefit resulting from the application of subsection 21(2) of the *PBSA* (the 50% rule)[2] must be included in the annual pension benefit payable.

[2] Subsection 21(2) provides that excess contributions with interest be applied to increase the pension benefit to the member as it is part of the deferred or immediate pension benefit

Delegations and Transfers between Jurisdictions

Pension plans which cover both employees subject to federal pension legislation as well as members subject to provincial legislation are known as multi-jurisdictional pension plans. Over the years, the Minister of Finance has entered into a number of reciprocal or bilateral agreements with most provincial pension authorities. According to these agreements multi-jurisdictional pension plans may be registered where the plurality of members are employed. The reciprocal agreements enable:

- OSFI to administer the province's pension legislation on their behalf for members subject to that province's jurisdiction.
- Provincial regulators to supervise on behalf of OSFI for members subject to the *PBSA.*

Currently, there is no reciprocal agreement with Newfoundland and Labrador and the agreement with Quebec covers only members employed in the Northwest Territories, Yukon and Nunavut. Therefore, federally registered plans with members in Quebec and/or Newfoundland and Labrador who are not in included employment must ensure that the plan is registered with both OSFI and Quebec and/or Newfoundland and Labrador.

It is expected that plan administrators should know if their plans have members whose employment is subject to provincial jurisdiction and administer their plans accordingly. They should also report the breakdown of membership in the Annual Information Return (AIR).

Transfers of supervisory jurisdiction occur when the plurality of membership in a plan changes from one jurisdiction to another. If a plan administrator discovers that the plurality of membership has changed within the plan, they should contact their Relationship Manager to discuss the possibility of a transfer in supervisory jurisdiction. If a transfer in supervisory jurisdictions is required, the date of transfer will be determined through an administrative agreement between the two jurisdictions (regulators), and the plan administrator will be required to advise its membership.

Portability Options

On cessation of membership or plan termination, members not yet eligible to retire (or their survivors) are, except where the exercise of portability impairs the solvency of the plan, entitled to all portability options described in the *PBSA* and the *Pension Benefits Standards Regulations (PBSR)*. Members eligible to retire (or survivors) may be entitled to these portability options depending on the terms of the plan. Terminating members (or survivors) must be provided with their options within 30 days of ceasing membership in the plan and must be given at least 60 days to choose an option.

The transfer options available to members (or survivors) are:

- A cash refund if the pension benefit credit is not locked-in;
- Transfer of the pension benefit credit to another pension plan willing to accept the funds;
- Transfer of the pension benefit credit to a locked-in Registered Retirement Savings Plan (RRSP) or Life Income Fund (LIF), or Restricted Life Income Fund (RLIF), or
- Purchase an immediate or a deferred life annuity.

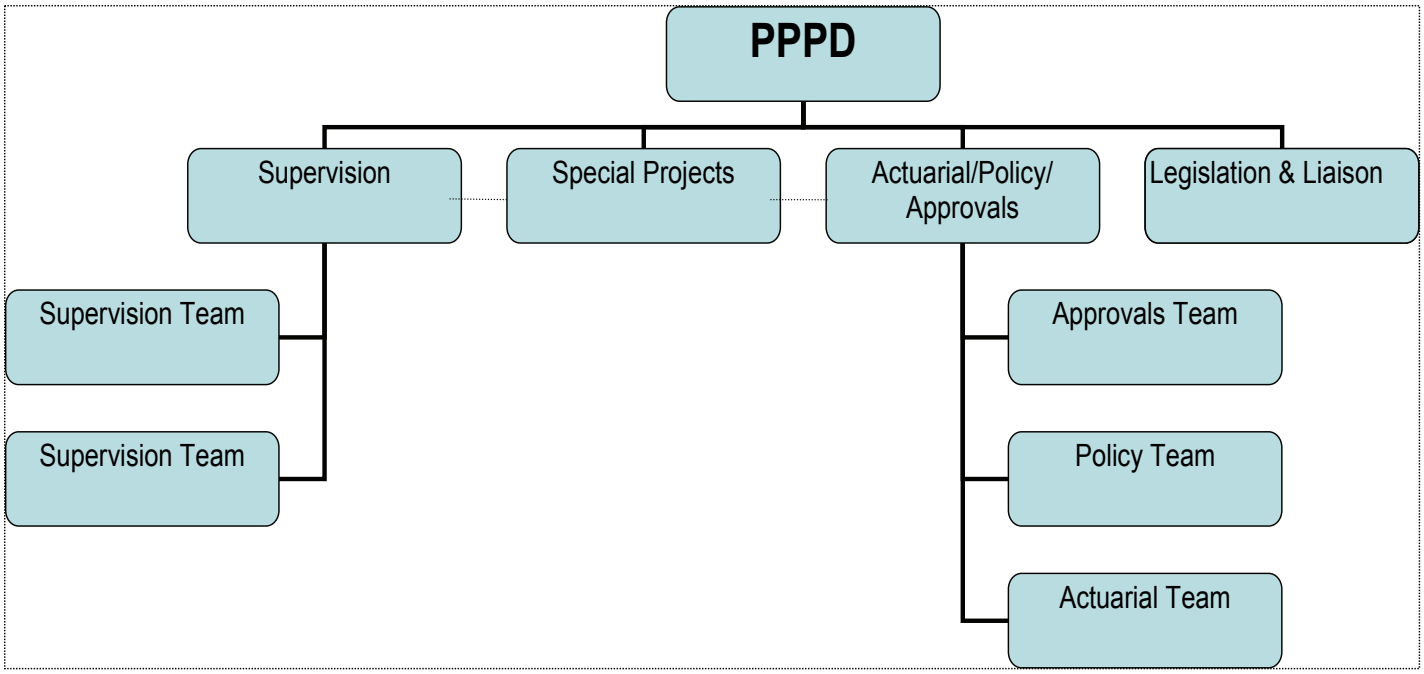
The *Income Tax Act* imposes a limit on the amount of money that can be transferred on a tax-sheltered basis and the *PBSA* permits the amount in excess of this limit to be unlocked and transferred out in cash.

Supervision Function within the Private Pension Plans Division (PPPD)

OSFI's mandate in relation to pension plans is to strive to protect the rights and interests of plan beneficiaries through the effective administration of the PBSA and the promotion of policies and procedures aimed at controlling risk.

OSFI is committed to improving communication about its mandate and the supervision of pension plans subject to the PBSA. InfoPensions – Issue 2 contained information on some of OSFI's supervisory activities including articles on interventions based on ESR results and the process for on-site examination findings and recommendations. This article will focus on the overall supervisory function within PPPD.

PPPD is organized by operational lines as shown in this chart.



The Supervision function within PPPD is delivered by teams of Relationship Managers (RMs) who monitor the administration and financial position of private pension plans subject to the PBSA.

Supervision staff support the achievement of OSFI's mandate by conducting risk assessments of pension plans, as outlined in the Risk Assessment Framework. This Framework and the associated Guidance Notes were published in April 2009 to enhance the transparency of the supervisory methodology that is applied to private pension plans. The Risk Assessment Framework is risk-based, meaning that it assists PPPD in identifying plan risks early and allocating resources to higher risk plans. It continues to place the onus on plan administrators to administer their pension plans in compliance with the PBSA.

The following provides additional detail on some of the supervisory activities within the Risk Assessment Framework:

Assessment of risk indicators

RMs use a series of indicators to assess risks. These risk indicators are based on information collected through required regulatory filings, custodian alerts, market information as well as plan sponsor and industry information. The risk indicators apply to all pension plans subject to the PBSA and are classified into three tiers according to the significance of the risks.

See Supervision Function on Page 5

Supervision Function within the Private Pension Plans Division (PPPD) (cont'd)

- A high risk indicator is one that may signify that promised benefits are in jeopardy such as non-remittance of contributions or an employer facing serious financial issues;
- Above average risk indicators include late filing of the actuarial report or a large portion of available surplus is being used towards a contribution holiday;
- A medium risk indicator may identify possible poor governance practices such as a history of late filings or reoccurring investment losses.

The level of intervention taken by OSFI is dependent on the level of risk(s) identified and therefore a high risk indicator would trigger immediate action by OSFI and a more in-depth review of the plan. RMs will discuss the risks identified with plan administrators and will inform them of an imminent intervention in advance.

Review of actuarial reports

RMs review all actuarial reports that are filed with OSFI. If concerns are noted, the RM will refer the report to the Actuarial Team so that a more detailed analysis may be performed. Once the Actuarial Team has completed its review they will inform the plan administrator and plan actuary of issues identified in the report.

We expect plan actuaries to implement OSFI recommendations regarding the preparation of actuarial reports. For more details regarding OSFI's expectations please see our *Instruction Guide for the Preparation of Actuarial Reports for Defined Benefit Plans*.

Plan administrators' main point of contact at OSFI is the RM. Please contact your OSFI RM to discuss any questions you may have regarding the Risk Assessment Framework or our supervisory activities.

Preparation of Actuarial Reports – Designated Plans

Pension plans that meet the definition of a designated pension plan under Regulation 8515 of the *Income Tax Act (ITA)* are subject to the funding standards under the *PBSA and the Pension Benefits Standards Regulations, 1985 (PBSR)*.

OSFI expects plan actuaries to include the going concern and solvency valuations and funding requirements under the PBSA in actuarial reports for designated plans even if the reported contributions are constrained by the *ITA*.

For additional details of OSFI's expectations in the preparation of actuarial reports for designated plans please see our *Instruction Guide for the Preparation of Actuarial Reports for Defined Benefit Plans*.

2010 Pension Industry Forum

On February 17, 2010 OSFI held its first Pension Industry Forum in Toronto targeted to plan administrators of federally registered plans as well as actuaries, lawyers and other consultants. The Forum provided an overview of OSFI's priorities for the supervision and regulation of federally registered private pension plans. The Forum was well received with over 120 attendees. OSFI would like to thank everyone who attended, in particular to those who provided valuable feedback on the session. Copies of the presentations are available upon request.

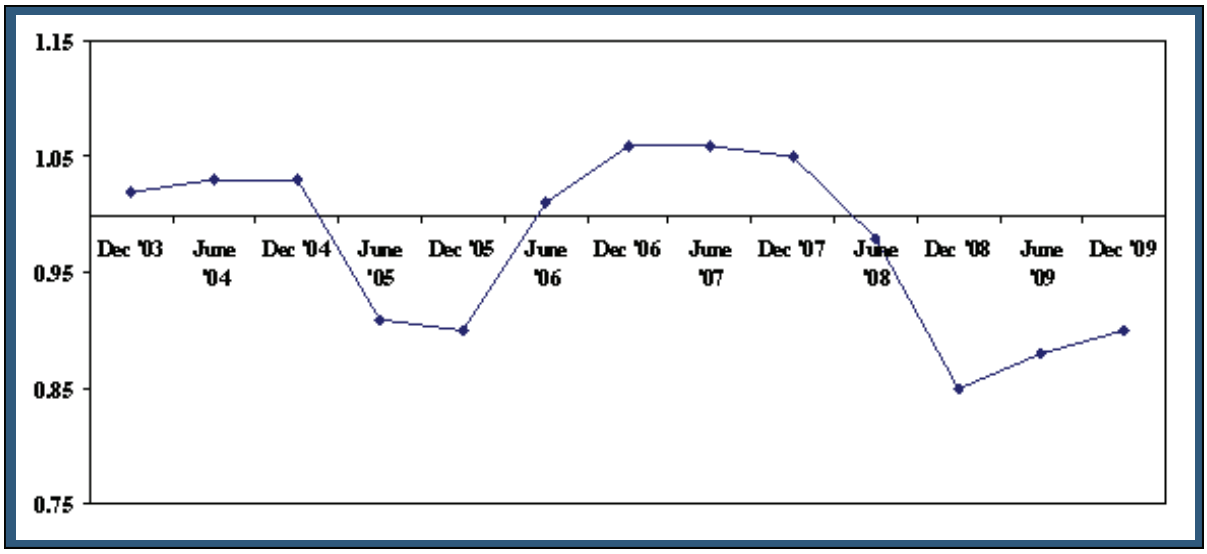
Estimated Solvency Ratio (ESR) Results and Charts

OSFI estimates solvency ratios for the approximately 400 defined benefit pension plans it regulates to assist with the early identification of solvency issues that could jeopardize the security of promised pension benefits.

The actual solvency ratio of a plan can differ from the ESR for a number of reasons. Please see *InfoPensions – Issue 2* for details on how OSFI calculates ESRs and our intervention activities based on these solvency testing results.

The weighted average ESR was 0.90 at December 2009. The average ESR at December 2009 shows a modest improvement over the ratio of 0.88 at June 2009.

Weighted average ESRs



OSFI estimated that 76% of the approximately 400 defined benefit plans were underfunded on a solvency basis at December 2009, compared to an estimated 79% at June 2009. At December 2009, only 15 % of all federally regulated pension plans had a solvency ratio of less than 0.80, whereas at the end of 2008, the comparable proportion was 40%.

Inactive Pension Plans

It has come to OSFI's attention that there may be instances where a certificate of registration has been issued by the Superintendent but no members are ever enrolled in the plan. Federally registered plans must be administered in accordance with the *PBSA* which includes the requirement to enrol employees eligible to join the plan, fund the pension plan and submit regular required filing. If a plan registered under the *PBSA* has never enrolled any members, the plan administrator should contact their Relationship Manager to discuss the status of the plan and whether or not to rescind the plan's registration under the *PBSA*. OSFI will continue to require filings until the plan is terminated or de-registered.

Provincial Property Laws

Section 25 of the *PBSA* provides that, subject to that section, applicable provincial property law will apply to pension benefits and pension benefit credits under a federal private pension plan. Provincial property law is the law of the province relating to the distribution of the property of spouses on divorce, annulment or separation or the property of former common-law partners and may include provincial pension legislation where that legislation relates to the distribution of property on the breakdown of a marriage or common-law partnership.

Section 25(4) of the PBSA also provides that, notwithstanding anything in provincial property law, the member can assign all or part of the member's pension benefit or pension benefit credit.

IFRS Update

The Accounting Standards Board (AcSB) confirmed that Canadian publicly accountable enterprises (PAEs) are moving to International Financial Reporting Standards (IFRS). Although pension plans are considered PAEs, in February 2010 the AcSB approved Section 4600, *Pension Plans*, as Part IV of the CICA Handbook. These standards will be effective for interim and annual financial statements relating to fiscal periods beginning on or after January 1, 2011, with early application permitted. OSFI will review these standards and assess whether changes are necessary to the existing Certified Financial Statements (OSFI-60). OSFI expects pension plans to continue filing the OSFI-60 form, and the accompanying auditor's report, in accordance with the existing Guide to the Certified Financial Statements until further notice.

Custodial Transfers within a Pension Fund

OSFI would like to remind administrators that changing the custodian of a pension fund is not considered an asset transfer under Section 10.2 of the *PBSA* and therefore does not require the Superintendent's permission. However, when a custodial change within a pension fund occurs, supporting documentation, such as a new trust agreement or insurance contract and new account number, must be filed with OSFI. Plan administrators must also inform the new custodian of the pension fund of all amounts that are to be remitted to the pension fund and the expected date of the remittance as per subsection 9.1(1) of the *PBSA.*

Pension Plan Documentation filed with OSFI

OSFI sometimes receives documentation from plan administrators labelled as "Personal and Confidential" or "to be opened by addressee only". Since a plan administrator's main point of contact at OSFI is the Relationship Manager (RM), the RM is frequently the addressee for plan documentation received by our office. We would like to reassure pension plan stakeholders that all documentation filed with our office is handled professionally by staff with all due respect for confidentiality. However, documentation filed with our office regarding a private plan subject to the *PBSA* becomes the information of OSFI, and hence is not "Personal and Confidential" to the RM. We therefore ask that this label be avoided when filing documentation with OSFI.