To Fund or Not to Fund for Solvency – Who Gets the Breaks?

by Ken Burns and Meghan Popp

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FUNDING

To Fund or Not to Fund for Solvency – Who Gets the Breaks?

*Kenneth E. Burns**
Meghan Popp
Lawson Lundell LLP

The first decade of the 21st century has seen a sea of change in the funded status of many defined benefit pension plans. Whereas the century began with many employers seeking ways to withdraw surplus funds from their pension plans, it took a very short time for many of these surpluses to disappear and turn into deficits. Behind the scenes, we have witnessed plans whose funding requirements were driven by going concern valuations flip topside to see their funding requirements driven by solvency valuations and their short five-year amortization period.

This article looks at what the different Canadian jurisdictions have done in recent years to address these solvency funding pressures. Some jurisdictions have responded with rules that permit plan sponsors to use letters of credit to temporarily plug solvency deficiencies, while others have permitted moratoriums on solvency special payments, or extended amortization periods, usually accompanied with requirements for member consent. While single employer private sector pension plans never get a complete exemption from solvency funding, some public sector plans do enjoy such exemptions. Increasingly, funding relief measures are also being tailored to suit private sector multi-employer plans, provided certain specified conditions are met.

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Jurisdiction by Jurisdiction Comparison

The paragraphs that follow summarize how the federal government and different provinces deal with solvency funding relief.

British Columbia

The *Pension Benefits Standards Act*[1] and the *Pension Benefits Standards Regulation*[2] require that defined benefit pension plans be funded on a solvency basis.[3] However, the four core public sector pension plans in British Columbia – the Municipal, College, Public Service and Teachers' pension plans – are exempt from performing a solvency valuation and making special payments in respect of any solvency deficiencies pursuant to section 3(10) and Schedule 1 of the *Pension Benefits Standards Regulation*.[4]

The broader public sector pension plans and most multi-employer plans in British Columbia are not exempt from the solvency funding requirements in the *Pension Benefits Standards Act*. The only relief available to these plans is the option to use a letter of credit to fund their solvency deficiencies.[5]

There is a temporary exemption available for certain negotiated cost plans, which are administered by two or more non-affiliated employers and the employer contributions are fixed by contract, provided they meet certain criteria. Under Schedule 1.1 of the *Pension Benefits Standards Regulation*, such plans may apply to the Superintendent for a moratorium on the special payment required for any solvency deficiencies for a period of up to three years. Such applications must be made prior to December 31, 2013.

Alberta

The *Employment Pension Plans Act*[6] applies to all pension plans in the province,

[1] R.S.B.C., c. 352 ("B.C. PBSA").
[2] B.C. Reg. 433/93 ("B.C. PBSR").
[3] B.C. PBSA, s. 40; B.C. PBSR, s. 35.
[4] Schedule 1 states that each of the four plans is exempt from B.C. PBSA, s. 41 and B.C. PBSR, s. 35. *Public Sector Pension Plans Act*, S.B.C. 1999, c. 44, Schedule A, s. 12 requires the College pension plan to perform "going concern" actuarial valuations and to act on the recommendations contained in the resultant reports.
[5] B.C. PBSR, s. 35.1.
[6] R.S.A. 2000, c. E-8 ("EPPA").

including both private and public sector plans. It requires most plans to fund on a solvency basis. However, core public sector pension plans in Alberta[7] are exempt from these rules because a separate statute, the *Public Sector Pension Plans Act*,[8] substitutes its own funding requirements. The latter legislation expressly exempts the core public service plans from having to comply with the solvency funding rules in the *Employment Pension Plans Act*.[9] Instead, it requires the adjustment of contribution rates for current service so that those rates will meet the solvency funding requirements.[10]

Under the *Employment Pension Plans Regulation*,[11] broader public sector plans are also exempt from some of the solvency funding requirements. Schedule 0.1 of the *Employment Pension Plans Regulation* specifically exempts the Universities Academic Pension Plan from the solvency funding requirements. Instead, the plan is required to perform an actuarial valuation at least once every three years and increase the contribution rates, if necessary, to meet the funding requirements.

Schedule 0.2 provides other publicly funded pension plans with exemptions from the solvency funding requirements if they meet the definition in section 2(*q*.1) of the *Employment Pension Plans Regulation*. Such plans may apply for these exemptions as long as the participating employers agree to fund any shortfall on plan wind-up if the plan should ever be discontinued.[12]

The *Employment Pension Plans Regulation* also permits specified multi-employer pension plans ("SMEPPs") (plans administered for employees of two or more non-affiliated employers) to apply to the Superintendent to temporarily suspend required solvency payments if certain conditions are met.[13] Initially, this regulation provided for a three-year moratorium, which ran out in 2008. However, a recent amendment permits SMEPPs whose three-year period ran out in 2008, or SMEPPs that had not previously applied for relief, to apply for a three-year moratorium from solvency deficiency payments any time before January 1, 2012.

Saskatchewan

The Pension Benefits Act, 1992[14] and its regulations contain solvency funding requirements in respect of all defined benefit plans which are registered under the Act.[15] In September 2009, the Saskatchewan government amended the regulations to provide temporary relief from solvency deficiency funding in the form of a three-year moratorium on solvency payments.

However, *The Pension Benefits Act, 1992* does not apply to the core public sector plans established by the Saskatchewan government for its own employees.[16] These plans do not have a solvency funding requirement;[17] instead, any deficiencies in the plan are paid out of the province's General Revenue Fund and are the responsibility of the government of Saskatchewan.[18]

Saskatchewan's broader public sector plans and multi-employer plans are subject to the solvency funding requirements of *The Pension Benefits Act, 1992*. Accordingly, they may also apply for the temporary relief provided for in the regulations and available to all defined benefit pension plans.

Manitoba

Manitoba's pension standards act is *The Pension Benefits Act*.[19] Like in other jurisdictions, it requires registered plans to fund on a solvency basis. Despite this, section 4.5(2) of

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[7] These include the Local Authorities Pension Plan, Management Employees Pension Plan, Public Service Pension Plan, Special Forces Pension Plan, and Provincial Judges and Masters in Chambers Pension Plan, as well as other supplemental and closed plans.

[8] R.S.A. 2000, c. P-41 ("Alta. PSPPA").

[9] See Alta. PSPPA, Schedule 1, s. 1(1)(*b*).

[10] See Alta. PSPPA, Schedule 1, s. 5.

[11] Alta. Reg. 35/2000 ("EPPR").

[12] EPPR, section 68(5) and Schedule 0.2.

[13] EPPR, Schedule 0.2(3).

[14] S.S. 1992, c. P-6.001 ("Sask. PBA").

[15] Sask. PBA, s. 40 and *Pension Benefits Regulations, 1993*, R.R.S. c. P-6.001 Reg. 1, ss. 36 to 36.6.

[16] These include the Public Service Superannuation Plan; Teachers' Superannuation Plan; SaskPower Superannuation Plan; Liquor Board Superannuation Plan; Members of the Legislative Assembly Superannuation Plan; and Judges of the Provincial Court Superannuation Plan.

[17] See *The Public Service Superannuation Act*, R.S.S. 1978, c. P-43.

[18] PBA Defined Benefit Annual Reports for fiscal year ended March 31, 2010 at 12.

[19] C.C.S.M. c. P32 ("Man. PBA").

The Pension Benefits Regulation[20] exempts the core public sector pension plans created under *The Civil Service Superannuation Act*[21] and *The Teachers' Pensions Act*[22] from the solvency funding requirements set out in that regulation and *The Pension Benefits Act.*

Manitoba has also recently granted solvency exemptions to broader public sector plans under the *Solvency Exemption for Public Sector Pension Plans Regulation*,[23] which was registered on June 29, 2010. It provides for a permanent exemption from the solvency funding requirements to those public sector pension plans registered under *The Pension Benefits Act*. This new regulation enables a broader public sector pension plan to opt out of solvency funding requirements, subject to not more than 1/3 of members objecting.

With respect to all other pension plans, including multi-employer plans, Manitoba has also introduced the *Special Payments Relief Regulation*,[24] which allows defined benefit plans to elect to amortize special payments for solvency deficiencies over an extended ten-year period with member and beneficiary buy-in.

Ontario

Defined benefit pension plans in Ontario are subject to the funding requirements set out in the *Pension Benefits Act*[25] and its regulations.

Amendments to the *Pension Benefits Regulations* in 2007 temporarily exempted certain multi-employer plans from having to be funded on a solvency basis for a period of three years. These rules apply to plans that are designated as specified Ontario multi-employer pension plans ("SOMEPPs"),[26] meaning they have at least fifteen unaffiliated employers or are plans in which at least 10% of active members move from one participating employer to another each year, provide target benefits and meet certain other criteria, including an ability to reduce accrued benefits under the terms of the plan.

Further amendments passed in December 2010 exempt jointly sponsored pension plans in existence as of August 24, 2010 from solvency funding requirements, provided certain requirements are met, such as enhanced disclosure to members.[27] All the necessary criteria will not be known until the required regulations are released.

It is widely anticipated that the forthcoming regulations will also significantly change the SOMEPP rules. For example, it is anticipated that the regulations will make Ontario the first Canadian jurisdiction to offer permanent solvency funding relief to qualified multi-employer plans as opposed to the temporary moratoriums on such funding available in other jurisdictions.

On February 10, 2011, the Ontario government released proposed amendments to the *Pension Benefits Regulations*,[28] which will provide temporary solvency relief for certain public sector plans. In order to be eligible for this funding relief, plans must meet the definition of "public sector pension plan," which includes single-employer pension plans sponsored by Crown agencies and corporations, school boards, colleges, universities and municipalities. The plan must provide defined benefits and at least 25% of the total plan membership must be actively accruing benefits.

Recent amendments have also introduced letters of credit for funding solvency deficiencies.[29] However, public sector pension plans, other than those that may be specifically set out in the regulations, and multi-employer plans are expressly prevented from using letters of credit. This may be reflective of the government's intention to provide other forms of solvency relief for these types of plans.

Quebec

The *Supplemental Pension Plans Act* requires registered defined benefit plans to be funded on a solvency basis.[30] Effective

[20] Man. Reg. 39/2010 ("Man. PBR").
[21] C.C.S.M., c. 120.
[22] C.C.S.M., c. 720.
[23] Man. Reg. 81/2010.
[24] Man. Reg. 190/2008.
[25] R.S.O. 1990, c. P.8 ("Ont. PBA").
[26] R.R.O. 1990, Reg. 909, s. 6.0.1.

[27] Ont. PBA, s. 1(2.1) [not in force], introduced in *Securing Pension Benefits Now and for the Future Act, 2010*, S.O. 2010, c. 24.
[28] R.R.O. 1990, Reg. 909.
[29] Ont. PBA, s. 55.2 [not in force], introduced in *Securing Pension Benefits Now and for the Future Act, 2010*.
[30] R.S.Q., c. R-15.1, ss. 116-118, 123-133 ("SPPA").

January 1, 2010, new funding measures were introduced in the SPPA, including the requirement for every defined benefit plan to establish a provision for adverse deviation on a solvency basis,[31] permanent rules relating to the use of letters of credit to satisfy solvency funding obligations,[32] and the obligation to file annual actuarial valuations, except in certain circumstances.[33]

Core public sector pension plans (such as the Government and Public Employees Retirement Plan, the Pension Plan of Management Personnel and the Teachers Pension Plan) are not subject to the SPPA and are governed by separate statutes providing for their own funding requirements.

Registered pension plans in the municipal and university sectors, although registered under the SPPA, are exempted from funding on a solvency basis.[34] Notwithstanding this exemption, actuarial valuations must still determine the plans' financial position on a solvency basis.

New Brunswick

The *Pension Benefits Act* applies to all pension plans in the province, including both private and public sector plans.[35] Under the *General Regulation – Pension Benefits Act*, every defined benefit pension plan registered under the *Pension Benefits Act* is subject to solvency deficiency funding requirements.[36] Such deficiencies must be funded by special payments amortized over five years from the date the deficiency was identified.[37]

Funding relief is available in certain circumstances where the Superintendent of Pensions may reduce the special payment amount by extending the amortization period.[38] One such circumstance is where the special payments required have been rendered onerous as a result of liabilities for escalated adjustments having been taken into account in the first solvency valuation after January 31, 2001. An employer may also apply for an extended amortization period to a date on or before December 31, 2018. The request must be made within nine months of the actuarial valuation report filed and the actuary must certify that the plan has sufficient assets to meet its cash flow requirement during the extended amortization period. The employer must also give notice of the application to plan members and beneficiaries.[39]

In addition to the above, there are special provisions in the *General Regulation – Pension Benefits Act* for solvency relief unique to municipalities and universities. Subject to some conditions, municipalities and universities with defined benefit plans may apply for and obtain an exemption from solvency deficiency funding.[40] The employer or sponsor must give notice of the proposed funding exemption to the members and beneficiaries, who will have an opportunity to vote on the matter. If the proposal receives at least 51% in favour, the Superintendent can register the exemption.[41]

Nova Scotia

The *Pension Benefits Act* applies to every pension plan provided for persons employed in Nova Scotia.[42] The *Pension Benefits Regulations* require a pension plan to be funded for any going concern unfunded actuarial liabilities and any solvency deficiencies under the plan. Special payments to amortize a funding deficiency must be amortized over a period of fifteen years for going concern unfunded liabilities and five years for solvency deficiencies.[43]

The *Pension Benefits Regulations* also contain special provisions for universities and municipalities with respect to the amortization period for solvency funding. Under a university pension plan, a solvency deficiency which arose before January 1, 2006 may be

[31] SPPA, s. 128; *Regulation respecting supplemental pension plans*, R.R.Q., c. R-15.1, r. 1, ss. 60.1-60.5 ("SPPR").

[32] SPPA, s. 42.1, 123; SPPR, ss. 15.0.01-15.0.0.10.

[33] SPPA, s. 118.

[34] *Regulation respecting the funding of pension plans of the municipal and university sectors*, R.R.Q., c. R-15.1, r. 0.1.01. The pension plan for employees of early childhood centers and private day care centers is also exempted from funding on a solvency basis.

[35] S.N.B. 1987, c. P-5.1, ss. 2 and 3.

[36] N.B. Reg. 91-195, s. 35(1) ("N.B. PBR").

[37] N.B. PBR, ss. 35(2)(*c*) and 36(1)(*c*).

[38] N.B. PBR, s. 36(1.1).

[39] N.B. PBR, s. 36(1.2).

[40] N.B. PBR, s. 42.1(1).

[41] N.B. PBR, s. 42.1(2)-(4).

[42] R.S.N.S. 1989, c. 340, s. 4.

[43] N.S. Reg. 164/2002, ss. 6(1)(*b*) and (*d*)(i). ("N.S. PBR").

amortized over fifteen years.[44] Municipalities are not provided the same increased amortization period; however, there are special provisions which allow municipalities to reduce the amount of any special payment required to fund to 85% solvency over the usual five-year period.[45]

In 2010, the *Pension Benefits Regulations* were amended to introduce additional provisions for temporary solvency funding relief for all pension plans. Pension plans with solvency deficits identified on the first actuarial valuation report prepared between December 30, 2008 and January 2, 2011, may amortize the special payment amount required to fund the deficit over ten years instead of five years.[46] With this temporary relief are restrictions on what amendments can be made to the pension plan during the first five years of the ten-year amortization period.[47]

Universities with existing solvency deficits in their pension plans before January 2, 2011 are exempt from making special payments for the first year after the first actuarial valuation report prepared between December 30, 2008 and January 2, 2011. Payments made following that one-year exemption may be amortized over nine years.[48] The same relief is available to specified multi-employer pension plans.[49]

Under the temporary solvency relief provisions, municipalities may continue to fund solvency deficits to 85% solvent instead of 100%. The amortization period was similarly increased to ten years from the usual five-year period.

The temporary solvency relief provisions also require the employer to provide notice of their intention to change the special payments, including a statement that special payments will not be changed under these provisions if 1/3 or more of the members, former members or other beneficiaries object.[50] For specified multi-employer pension plans, notice is required but members are not given the opportunity to object.

Prince Edward Island

There is currently no pension benefits legislation in force in PEI, and as such, there are no minimum funding requirements. However, on December 1, 2010, Bill 30, the *Pension Benefits Act*, received its first reading in the PEI legislature.[51] As it stands, the Bill, which is virtually identical to the Nova Scotia *Pension Benefits Act*, will apply to all pension plans provided for persons employed in the province. Once enacted, the Bill will repeal PEI's previous *Pension Benefits Act*, which was enacted in 1990 but never proclaimed.

The PEI government has indicated that Bill 30 will undergo an extensive consultation process with stakeholders before its second reading, which the government suggests may occur in the spring of 2011.[52] Given the consultation process, it is likely that solvency funding will be a key topic of concern among plan sponsors. A consultation paper issued by the government invites discussion on all aspects of the legislation, but does not specifically address solvency funding.[53]

Newfoundland and Labrador

Newfoundland and Labrador's *Pension Benefits Act 1997*[54] applies to all plans for persons employed in the province. However, public sector plans are exempt from the solvency funding requirement of the Act pursuant to section 41 of the *Pension Benefits Act Regulations*.[55]

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[44] N.S. PBR, s. 6(1)(*d*)(ii).

[45] N.S. PBR, s. 6(1)(*d*)(iii) – for the remaining balance of any solvency deficiency which arose between December 30, 2005 and August 30, 2006, and any new solvency deficiency which arose after August 30, 2006 and before August 30, 2016, the municipality must fund that part of the solvency deficiency that is greater than 15% of the solvency liabilities within five years of the valuation date.

[46] N.S. PBR, s. 6A(3).

[47] N.S. PBR, s. 6A(4).

[48] N.S. PBR, s. 6A(3A).

[49] N.S. PBR, s. 8A(4B).

[50] *Pension Benefits Regulations*, s. 6A(5).

[51] Bill 30, *Pension Benefits Act*, 4th Sess., 63rd Leg., Prince Edward Island, 2010.

[52] The Government of Prince Edward Island, Justice & Public Safety, news release, "Government Introduces Pension Benefits Act" (December 2, 2010) online: http://www.gov.pe.ca/index.php3?number=news&newsnumber=7483&dept=&lang=E.

[53] The Government of Prince Edward Island, *Consultation Paper: Bill 30*, Pension Benefits Act (December 3, 2010), online: http://www.gov.pe.ca/photos/original/PensionBenefits.pdf.

[54] S.N.L. 1996, c. P-4.01.

[55] N.L.R. 114/96 9 ("Nfld. PBR").

On June 12, 2008, Newfoundland and Labrador announced the enactment of new *Solvency Funding Relief Regulations*,[56] which offer two avenues of temporary funding relief to regular defined benefit plans where the plan is subject to an "initial solvency deficiency" based on actuarial valuation reports completed between January 1, 2007 and January 1, 2009.[57] The *Solvency Funding Relief Regulations* were made retroactive to January 1, 2007, and as it stands, will be repealed effective February 1, 2019.[58]

The first option provided by the *Solvency Funding Relief Regulation* allows eligible plans to consolidate previous solvency funding payment schedules by special payments sufficient to liquidate the deficiency by equal annual payments over a five-year period.[59] Under the second option, the solvency funding period can be extended to ten years, provided that less than 1/3 of active plan members or non-active members and beneficiaries, including retirees, object, or the difference between the five-year and ten-year level of payments is secured by letter of credit.[60]

The *Solvency Funding Relief Regulations* do not apply to multi-employer pension plans.[61] However, by amendment to *Pension Benefits Act Regulations*, multi-employer pension plans can elect a one-time exemption from solvency funding based on actuarial valuation reports completed between December 31, 2007 and December 31, 2010.[62] Under such election, required contributions will be sufficient if they are not less than the sum of: (a) the normal cost of the plan; (b) the special payments set out in a previous report that remain to be paid with respect to any going concern unfunded liability; and (c) the special payments to be paid with respect to a going concern unfunded liability that is determined in the report.[63]

Newfoundland and Labrador have also granted plan-specific exemptions to the Memorial University Pension Plan and the Newfoundland and Labrador Municipal Employees Benefits Inc. Pension Plan, pursuant to sections 41(4) and 42.2 of the *Pension Benefits Act Regulations*.

Federal

Like provincial pension legislation, the *Pension Benefits Standards Act, 1985*[64] contains solvency funding requirements. Also like in many provinces, core public sector pension plans – in the case of the federal government, the pension plans for the Public Service, Canadian Forces and RCMP – are exempt from these requirements.[65] The funding requirements of these public sector plans are based on the specific acts which create and govern them. Each requires only going concern considerations.

The Public Service Superannuation Plan is governed by the *Public Service Superannuation Act*.[66] The federal government is the sponsor of the plan and has always assumed responsibility for the cost of benefits that exceed the regular contributions made by employees and the government. Thus, the government makes up any deficits that occur when actual plan costs differ from the actuarial assumptions used to determine the necessary government contributions. The *Public Service Superannuation Act* requires that actuarial deficiencies in the pension fund be dealt with by transferring equal installments to the fund over a period not exceeding fifteen years. For the period prior to April 1, 2000, a separate market invested fund was not maintained; however, the *Public Service Superannuation Act* provides that all pension obligations arising from the plan be met by the government by increasing the Public Service Superannuation Account in equal installments over a period not exceeding fifteen years.

Likewise, both the *Royal Canadian Mounted Police Superannuation Act*[67] and the *Canadian Forces Superannuation Act*,[68] also require that actuarial deficiencies found in their pension funds to be dealt with by transferring amounts to the fund in equal

[56] N.L.R. 30/08 ("Nfld. SFRR").
[57] Nfld. SFRR, s. 2(*g*), 3, 5.
[58] Nfld. SFRR, ss. 28, 29.
[59] Nfld. SFRR, s. 6.
[60] Nfld. SFRR, s. 7.
[61] Nfld. SFRR, s. 4(*b*).
[62] Nfld. PBR, s. 7.1.
[63] Nfld. PBR, s. 7.1.

[64] R.S.C. 1985, c. 32 (2nd Supplement) ("PBSA").
[65] PBSA, s. 4 and *Pension Benefits Standards Regulations, 1985*, SOR/87-19, s. 4 and Schedule 1.
[66] R.S. 1985, c. P-36.
[67] R.S.C. 1985, c. R-11.
[68] R.S.C. 1985, c. C-17.

installments over a period not exceeding fifteen years and that deficiencies found between the balance of the respective Superannuation Accounts and the actuarial liability be reduced by increasing the Account in equal installments over a period not exceeding fifteen years.[69]

In 2006, the federal government announced temporary Solvency Funding Relief Regulations[70] under the *Pension Benefits Standards Act, 1985*, and then in 2009 renewed them with modifications in the *Solvency Funding Relief Regulations, 2009*.[71] These measures permit plans to extend solvency funding payment periods to ten years with either member and retiree support or with a letter of credit as security. Federal crown corporations are able to access the relief by direct application to the Minister of Finance and the payment of a fee.

Yukon, Northwest Territories, Nunavut

None of the territories has a pension standards statute. Instead, most pension plans established in the territories are subject to the federal *Pension Benefits Standards Act, 1985*,[72] and thus, the federal pension funding rules apply unless an exception provided for under the federal Act applies. Territories have the ability to enact their own public sector and broader public sector pension legislation which could (and presumably would) exempt such plans from solvency funding obligations. However, each territory's core public service currently participates in the federal Public Service Superannuation Plan alongside the federal public service.

[69] *Royal Canadian Mounted Police Superannuation Act*, ss. 29, 29.3 and *Canadian Forces Superannuation Act*, ss. 55, 55.3.
[70] SOR/2006-275.
[71] SOR/2009-182.

[72] PBSA, s. 4(4)(*i*).

LAWSON LUNDELL LLP

www.lawsonlundell.com

Vancouver

Suite 1600 Cathedral Place
925 West Georgia Street
Vancouver, British Columbia
Canada V6C 3L2
(T) 604.685.3456
(F) 604.669.1620

Calgary

Suite 3700, 205 - 5th Avenue S.W.
Bow Valley Square 2
Calgary, Alberta
Canada T2P 2V7
(T) 403.269.6900
(F) 403.269.9494

Yellowknife

P.O. Box 818
200, 4915 - 48 Street
Yellowknife, Northwest Territories
Canada X1A 2N6
(T) 867.669.5500
(F) 867.920.2206
Toll Free: 888.465.7608