Frequently Asked Questions Pertaining to the 2018 Funding Reform for Defined Benefit Pension Plans

New Ontario funding rules (O. Regulation 250/18) for defined benefit pension plans came into effect on May 1, 2018. The Financial Services Commission of Ontario (FSCO) has developed frequently asked questions (FAQs) and other communication materials to address questions concerning the new funding requirements.

The FAQs are organized as follows:

Provision for Adverse Deviations (PfAD)	
Background	
SIPP Content Provision	100 series
Actuarial Issues	200 series
Investment Classification	300 series
Transition Rules	400 series
Funding Related Disclosures	500 series
Section 76(12) Investment Categories	Exhibit 1

FSCO has also developed a series of other communications on the new funding rules, which can be found on the general 2018 Funding Reform page.

Provision for Adverse Deviation (PfAD)

Background

On May 1, 2018, a new funding regime came into effect for Ontario single employer pension plans. This includes a change to the solvency funding rules and the introduction of a new funding provision for adverse deviations (PfAD). The PfAD is prescribed in section 11.2 of Regulation 909, and provides for an additional level of funding on top of existing normal cost and going concern funding requirements. The PfAD is based on a number of factors, including the asset allocation of the plan, the discount rate, and whether any portion of the plan is closed to new members.

The new regime also introduced a new disclosure requirement for the statement of investment policies and procedures (SIPP), set out in sections 78(7) and (8) of Regulation 909. It requires that the SIPP include the plan's target asset allocation for each of the investment categories listed in section 76(12) (see the list of categories attached in Exhibit 1).

FAQs on the new PfAD and SIPP regulations are provided below.

There are optional transition provisions regarding the calculation of component "B" of the PfAD, as prescribed under sections 11.2(11) and (12) of Regulation 909, that apply to valuation reports with a valuation date before December 31, 2019. See FAQ series 400 in this regard.

SIPP Content Provisions

Q100. What are the new requirements under sections 78(7) and (8) of Regulation 909 and what steps must I take to comply?

A100. Section 78(7) of Regulation 909 requires that the SIPP include the plan's target asset allocation for each of the investment categories listed in section 76(12) of Regulation 909. Section 78(8) describes the target asset allocation for an investment category as the target proportion of the plan's assets invested in a particular investment category in proportion to the total target investment in all investment categories, expressed as a percentage.

To comply with this requirement, the administrator can either amend the existing target asset allocation in the SIPP to reflect the investment categories in section 76(12) of Regulation 909, or create a second asset allocation table that provides the required target asset allocations.

Where a separate table is established to comply with sections 78(7) and (8), the plan's actual asset allocation is governed by both the original description of the target asset allocation already found in the SIPP and the description of the target asset allocation in the separate table.

FSCO recognizes that it may take time for the administrator to review and amend the SIPP to meet the requirements of sections 78(7) and (8) of Regulation 909. FSCO expects the administrator to bring the SIPP into compliance with sections 78(7) and (8) of Regulations 909 as soon as is practical.

In any event, the plan's SIPP must contain the required asset allocation information on or before the valuation date of a report based on that information (i.e., December 31, 2019 or earlier).

Q101. Do the new SIPP requirements in sections 78(7) and (8) of Regulation 909 require every investment category in section 76(12) of Regulation 909 to be listed in the SIPP, even if there are no investments in that category?

A101. For purposes of sections 78(7) and (8) of Regulation 909, a SIPP does not need to explicitly list an allocation to an investment category in which the plan does not invest. Investment categories will be deemed to have no allocation if not mentioned in the SIPP.

Q102. Is it acceptable for the target asset allocation to be listed as a range? Is there any restriction on the ranges that can be specified in a SIPP?

A102. Under section 11.2(8) of Regulation 909, the PfAD is to be based on the target asset allocation as documented in the plan's SIPP, and requires a single figure expressed as a percentage for each section 76(12) investment category in which the plan invests. A range would not work for purposes of the PfAD calculation, but can be included in the SIPP in addition to the target (as is commonly done).

With respect to the second part of this question, there is no specific restriction on the asset allocation ranges that can be specified in the SIPP. However, an overly wide asset allocation range may not provide necessary investment control and monitoring of that asset category.

We also make note of the *Guideline for the Development of Investment Policies and Procedures for Federally Regulated Pension Plans*, published by the Office of Superintendent of Financial Institution, which provides useful guidance on developing investment policy, and advises that the range of possible allocations should be sufficiently narrow so that:

- the intentions of the administrator are clear;

- the activities of investment managers can be controlled; and
- third parties can assess the security of benefits.

Q103. Section 78(7) of Regulation 909 requires the SIPP to state target allocations for each of the asset categories in section 76 (12) of Regulation 909. For plans that invest entirely in pooled funds, how would the requirement in section 78(7) be applied?

A103. FSCO recognizes that a pooled fund is an investment vehicle, and not strictly speaking an asset class. There are two acceptable approaches to addressing pooled funds in the target asset allocation in the SIPP.

Under the first approach, the SIPP does not have to specify an allocation to pooled funds (investment category 2), even if the plan ultimately employs these vehicles. The SIPP can instead set out its target asset allocations using the other investment categories listed in section 76(12). In doing so, the administrator is indicating that it does not allocate any assets to pooled funds as an asset class, although it may use pooled funds to achieve its allocation to the investment categories that are indicated.

Under the second approach, the administrator may decide to indicate that it has allocated all (or a stated portion) of its assets to the "pooled fund" investment category. If it takes this approach, then the SIPP must also indicate what the underlying allocation is to the various investment categories listed in subsection 76(12) in order to permit the calculation of the PfAD in accordance with the look-through rules set out in section 11.2(8) of the Regulation. (The definitions of "N", "P" and "Q" in section 11.2(8) of Regulation 909 require the administrator to "look through" assets invested in pooled funds, and determine the proportion of those assets that are invested in investment categories "L" and "M", as defined in section 11.2(8)).

Where applicable, the SIPP should specify that the fund is permitted (or required) to invest plan assets using pooled funds.

Q104. Section 11.2(10) of Regulation 909 requires the use of the target asset allocation in the SIPP that "is in effect at the time at which the determination is made". What does "in effect at the time" and "at which the determination is made" mean?

A104. For the purpose of determining the PfAD, a SIPP is normally "in effect" either on the date it is approved or the date it is amended by the administrator. Where a SIPP specifically states a future effective date, the previous SIPP would still be considered to be "in effect" until that future date.

The phrase “at which the determination is made” is a reference to the valuation date of the report, and not the date the report was filed or signed.

Q105. If the SIPP calls for changes in the asset mix after the valuation date, should those future changes be reflected in the calculation of the PfAD?

A105. No. For the purpose of section 11.2(10) of Regulation 909, it is FSCO’s position that “the time at which the determination is made” refers to the valuation date of the valuation report. Future changes to the asset allocation noted in the SIPP, such as those in a de-risking glide path, that would occur after the valuation date of the report are not to be considered in calculating the PfAD.

This differs from the practice of setting the discount rate for purposes of the valuation report. In that case, the actuary needs to exercise professional judgement in reflecting any pending changes to the plan’s investments.

Actuarial Issues

Q200. For plans that have an explicit normal cost for expenses, should the PfAD be applied to this portion of the normal cost?

A200. For the purpose of the going concern valuation, the PfAD should be applied to any provisions for plan expenses payable from the pension fund.

Q201. Does the new provision for adverse deviations (PfAD) satisfy any margin requirement in the going concern discount rate noted in section 1 of FSCO’s Actuarial Guidance Note AGN-001?

A201. Effective May 1, 2018, the PfAD is a legislated additional funding target requirement under Regulation 909. In preparing a going concern actuarial valuation, the actuary needs to exercise professional judgement to determine whether an additional margin for conservatism is warranted; this includes, but is not limited to, taking into account the terms of engagement and relevant funding policy of the pension plan. For example, consideration should be given to whether there is a need or desire to build a funding buffer via additional margin for conservatism to enable plan stakeholders to better manage the volatility of funding obligations or sustainability of the plan's benefits in a going-concern context. Also, the actuary is expected to provide a rationale in the valuation report for any changes in assumptions, including any changes in margins. FSCO will undertake a review of our Actuarial Guidance Notes and revise as appropriate to reflect the requirements of the new funding regime.

Q202. When is a plan considered to be a "closed plan" for purposes of section 11.2 of Regulation 909?

A202. A "closed plan" is defined in section 11.2(1) of Regulation 909 as follows:

> "closed plan" means a pension plan at least one portion of which, according to the terms of the plan, does not permit new members to join and accrue defined benefits;"

Determining if a plan is "closed" requires analysis of the particular facts of that plan. Ultimately, it is the administrator who is responsible for making that determination and directing the actuary in that regard.

FSCO does not expect administrators or their advisors to request FSCO's determination of whether a particular plan is a closed plan; administrators are expected to make this determination, and to obtain any advice they may need to do so. If FSCO has reason to question a statement in an actuarial valuation report that a plan is not a closed plan, we may ask the signing actuary to provide the facts and analysis that support the administrator's determination in this regard.

Refer to the FSCO position paper *The determination of whether a plan is a "Closed Plan",* which provides some examples of whether a plan is "closed" or not in accordance with the definition in section 11.2(1).

Investment Classification

The questions below address the classification of certain investments for the purposes of calculating the provision for adverse deviations (PfAD). FSCO expects that the administrator, in consultation with its agent(s), will determine the appropriate classification of the investment or asset class. Both the administrator and, where applicable, its agent(s) should be prepared to justify any classification.

Q300. How would an investment in a real estate investment trust (REIT) be classified for purposes of determining the PfAD?

A300. The classification of an investment in a REIT will depend on the nature of the investment. For example, an interest in a REIT which is held through shares in a corporation would be classified as either investment category 13 or 14 of section 76(12) of Regulation 909, depending on whether it is a domestic or foreign corporation, and assuming none of the investment categories in paragraphs 1 to 12 apply. However, an interest in a REIT which is held through some other legal structure, such as a partnership or trust agreement, would be classified as investment category 17 (assuming none of the categories in paragraphs 1 to 16 of section 76(12) apply). As an investment in a REIT is not a direct investment in real estate, it would not be classified as investment category 7.

Q301. What is a real estate debenture as referred to in investment category 8?

A301. For purposes of section 76(12), "real estate debenture" (investment category 8) can be defined as a debt obligation backed by the credit of the real estate property owner, not by the collateral of the real estate property itself. Investment category 8 is classified as an "M" item under section 11.2(8) of Regulation 909.

Q302. Is private equity a "stock" and hence a non-fixed income asset under the PfAD rules, or is it not a stock, and hence falls under investment category 17 and is categorized as an "M" investment?

A302. The classification of a private equity investment will depend on the nature of the investment. For example, private equity that is accurately characterized as venture capital should be classified as investment category 10 (venture capital). Private equity that is in the form of Canadian or foreign "stock" (and is not venture capital) should be classified as either investment category 13 or 14 (Canadian or foreign stocks), depending on whether it is a domestic or foreign corporation and assuming none of the categories in paragraphs 1 to 12 of section 76(12) apply.

Q303. What is meant by the term "insured contracts" in section 76(12) of Regulation 909 and the term "benefits for which an annuity contract has been purchased from an insurance company" as used in sections 11.1 and 11.2 of Regulation 909?

A303. It is FSCO's view that "insured contracts" referred to in section 76(12) of Regulation 909 and the term "benefits for which an annuity contract has been purchased from an insurance company” which is used in sections 11.1 and 11.2 of Regulation 909 both refer to the same thing: buy-in annuities and buy-out annuities that are not subject to a discharge under section 43.1 of the PBA.

Buy-out annuities that are subject to a discharge under section 43.1 of the PBA, however, should no longer be included in the assets or liabilities of the plan, and therefore would not need to be included in the PfAD calculations.

Q304. How should infrastructure investments be treated under the PfAD rules?

A304. The classification of an investment in infrastructure will depend on the nature of the investment. For example, an investment in the shares of a Canadian infrastructure enterprise would be classified as either investment category 13 or 14 (Canadian or foreign stocks), depending on whether it is a domestic or foreign corporation, and assuming none of the categories in paragraphs 1 to 12 of section 76(12) apply. However, an interest in infrastructure which is held through some other legal structure, such as a partnership or joint venture, would be classified as investment category 17, assuming none of the categories in paragraphs 1 to 16 of section 76(12) apply.

Q305. How are commodities treated under the PfAD rules?

A305. The classification of an investment in commodities will depend on the nature of the investment. For example, the purchase of actual gold, or of gold futures, for example, would be classified as investment category 17 (other investments). Alternatively, the investment may take the form of an investment in the shares of a company that produces the commodity (e.g., mining company), in which case the investment would be classified as investment category 13 or 14 (Canadian or foreign stocks), depending on whether it is a domestic or foreign corporation, and assuming none of the categories in paragraphs 1 to 12 of section 76(12) apply.

Q306. Derivatives and leverage strategies can have an impact on the overall return/risk profile for the pension fund. However, the methodology for calculating the PfAD does not explicitly address their use. Are derivatives and leverage strategies to be considered in the PfAD calculations, and if so, how?

A306. Under sections 11.2(9) and (10) of Regulation 909, the PfAD is calculated using the plan’s target asset allocation as set out in the plan’s SIPP. Accordingly, the treatment of derivatives and leverage strategy will depend on how they are reflected in the target asset allocation, if at all.

Q307. If a bond held by a pension fund does not meet the minimum credit rating requirements, how is it treated under the PfAD rules?

A307. Under sections 11.2(9) to (10) of Regulation 909, the determination of the level of fixed income assets is not affected by any specific bond that is actually held in the portfolio. Instead, it depends on the target asset allocations to investment categories 15 and 16 (Canadian bonds and Foreign bonds), and whether the SIPP sets out a minimum rating for such category given by a credit rating agency recognized by a competent authority that is not less than the levels set out in the tables to section 11.2.

Q308. How is private debt treated under the PfAD rules?

A308. Private debt would fall into either investment category 15 or 16 (Canadian or non-Canadian bonds and debentures) assuming that none of the categories in paragraphs 1 to 12 of section 76(12) apply, but its treatment is subject to the credit rating requirement in section 11.2(9) of Regulation 909.

A target asset allocation in a plan's SIPP for investment category 15 or 16 is not considered fixed income unless the SIPP sets out a minimum rating for investments in that category that is given by a credit rating agency recognized by a competent authority that is not less than the levels set out in the tables to section 11.2.

Q309. What is meant by a "competent authority" in the phrase "by another credit rating agency recognized by a competent authority" as set out in sections 11.2(9) and (12) of Regulation 909?

A309. We understand that "competent authority" generally refers to a financial regulatory or supervisory authority recognized by legislation.

Q310. For private debt, can an internally developed credit rating from a third party investment manager be considered sufficient for the purpose of section 11.2(9) and (12) of Regulation 909?

A310. No.

Q311. If an investment grade bond was downgraded below the minimum credit rating as set out in the SIPP, would this impact the remaining investment grade bonds in the same investment category, so that they are no longer treated as 100% fixed income?

A311. No. A downgrading in the bond would not adversely affect the classification of the remaining investment grade bonds. However, the administrator would have to dispose of the bond within a reasonable period of time, in order to remain in compliance with its own SIPP.

Transition Rules

The following questions address the transition rules relating to component B of the PfAD formula, as prescribed under sections 11.2(11) and (12) of Regulation 909. These transition rules may be applied to valuation reports with a valuation date before December 31, 2019.

Q400. How do the transition rules work under sections 11.2(11) and (12) of Regulation 909?

A400. Under the transition rules, a plan's actual asset allocations to the section 76(12) investment categories on the valuation date of the report, as set out in the plan's financial statements, may be used instead of the plan's target asset allocations in determining the values of "L", "M", "N", "P", "Q" and "R" in section 11.2(8).

The transition rules may be used to calculate the PfAD in a valuation report with a valuation date before December 31, 2019.

Q401. Under the transition rules, how is a bond treated that does not meet the minimum credit rating requirements set out in section 11.2(12)? Does it impact other investment grade bonds in the same investment category?

A401. The bond would be classified as investment category 15 or 16 (Canadian or foreign bonds and debentures), depending on whether it is issued by a Canadian or foreign company, but would not be a fixed income asset for purposes of the PfAD calculation and would not be classified as an "L" or "M' investment (assuming that it does not fall under categories 1 to 12). The bond would not adversely affect the classification of the investment grade bonds held in the same investment category.

Q402. If a pooled fund has a small target allocation to high yield bonds (which would not meet the minimum credit rating referred to in section 11.2 of Regulation 909), how is the pooled fund treated for purposes of the PfAD under the transition rules?

A402. The definitions of "N", "P" and "Q" in section 11.2(8) of Regulation 909 require the administrator to "look-through" assets invested in pooled funds, and determine the proportion of those assets that are invested in investment categories "L" and "M", as defined in section 11.2(8).

Where the PfAD is calculated based on the actual asset allocation under the transition rules, the administrator, in consultation with its agent(s), can classify bonds individually.

Under this approach, if a pooled fund had 85% invested in investment grade bonds which meet the credit rating described in the regulations, and 15% high yield bonds that do not meet the credit rating, for purposes of calculating the PfAD, the actual bonds held in the pooled fund that meet the credit rating (i.e., 85%) would be treated as fixed income assets (i.e., included in "P"), and the bonds that do not meet the credit rating (i.e., 15%) would be treated as non-fixed income assets.

Q403. How is private debt treated under the transition rules?

A403. Under the transition rules, an investment in private debt that does not meet the minimum credit rating requirements in section 11.2(12) would not be considered a fixed income asset, and would not be classified as an "L" or "M' investment (assuming that it does not fall under categories 1 to 12). However, the private debt investment would not adversely affect the classification of the investment grade bonds held in the same investment category.

Q404. How are derivatives and leverage strategies considered in the PfAD, under the transition rules?

A404. Under the transition rules, the PfAD is calculated using the plan's actual asset allocation as set out in the plan's financial statements. Accordingly, the treatment of derivatives or a leverage strategy will depend on how they are reflected in the actual asset allocation in the financial statements, if at all.

Funding Related Disclosures

Q500. In any plan year where the employer is taking a contribution holiday, is the plan administrator required to notify the plan membership?

A500. If a plan administrator is taking a contribution holiday pursuant to section 7.0.3 of Regulation 909, section 8(4) of Regulation 909 requires the plan administrator to give notice to plan members, former members, retired members and trade unions and the advisory committee, if any, within the first six months of the fiscal year in which a planned contribution holiday is to occur. A separate notice to a member, former member or retired member is not required if the administrator includes the information required under section 8(3) in the annual or biennial statement provided to such member, former member or retired member in the same fiscal year.

Q501. Is section 4(1.3) of Regulation 909 only applicable to a report filed under the new rules?

A501. No. Section 4(1.3) provides that any amendment that is required for purposes of complying with 4(1.1) shall be made within 12 months after the date the first report with a valuation date on or after December 31, 2017, is filed. The regulation does not make a distinction as to whether the report was prepared under the old or new rules.

Q502. Under the new funding regime, new sections 40(1)(p)(v.1), 40.1(1)(m)(i.1) and 40.2(1)(l)(i.1) were added to the disclosure requirements and come into effect on January 1, 2019. What does this mean for plan administrators issuing statements to the plan membership on and after this date?

A502. The new disclosure provisions require the disclosure of the plan's estimated transfer ratio as at the end of the statement period and this requirement is to come into effect on January 1, 2019. This means that plan administrators must include these new disclosure requirements in statements (whether annual or biennial) issued on and after January 1, 2019.

Exhibit 1
Investment Categories for Purposes of Calculating the PfAD

The following table lists the categories in section 76(12) along with their classification under section 11.2(8) of Regulation 909 for purposes of calculating component B of the PfAD formula (as set out in section 11.2(2)). "L", "M", "N" and "R" are defined in section 11.2(8) (see also the following page). Assets in the "L" category are treated as fixed income, 50% of the assets in the "M" category are treated as fixed income. There are special "look-through" rules for assets in the "N" category. "R" assets are effectively excluded from the PfAD calculations.

Investment Category	Classification under 11.2(8)
1. Insured contracts.	R
2. Mutual or pooled funds or segregated funds.	N
3. Demand deposits and cash on hand.	L
4. Short-term notes and treasury bills.	L[1]
5. Term deposits and guaranteed investment certificates.	L
6. Mortgage loans.	M
7. Real estate.	M
8. Real estate debentures.	M
9. Resource properties.	M
10. Venture capital.	M
11. Corporations referred to in subsection 11 (2) of Schedule III to the federal investment regulations.	M
12. Employer issued securities.	No classification – treated as non-fixed income
13. Canadian stocks other than investments referred to in paragraphs 1 to 12.	No classification – treated as non-fixed income

14. Non-Canadian stocks other than investments referred to in paragraphs 1 to 12.	No classification – treated as non-fixed income
15. Canadian bonds and debentures other than investments referred to in paragraphs 1 to 12.	L1
16. Non-Canadian bonds and debentures other than investments referred to in paragraphs 1 to 12.	L1
17. Investments other than investments referred to in paragraphs 1 to 16.	M

1 Subject to the minimum credit rating requirements in sections 11.2(9) and (12) of Regulation 909.

Section 11.2(8) of Regulation 909 contains component B of the PfAD Formula. It states as follows:

(8) Subject to subsections (9) to (11), for the purposes of the value of "J" in subsections (4) and (7), the plan's combined target asset allocation for fixed income assets shall be determined in accordance with the formula,

$$L + (0.5 \times M) + (N \times P) + (0.5 \times N \times Q)] / (100\% - R)$$

in which,

"**L**" is the sum of the plan's target asset allocations for each of the investment categories listed in paragraphs 1, 3, 4, 5, 15 and 16 of subsection 76 (12), excluding any portions of the target asset allocations that are allocated to the assets described in "R", expressed as a percentage,

"**M**" is the sum of the plan's target asset allocations for each of the investment categories listed in paragraphs 6 to 11 and 17 of subsection 76 (12), excluding any portions of the target asset allocations that are allocated to the assets described in "R", expressed as a percentage, “**N**” is the plan’s target asset allocation for the investment category listed in paragraph 2 of subsection 76 (12), expressed as a percentage,

“**P**” is the proportion of “N” that is allocated to the investment categories listed in paragraphs 1, 3, 4, 5, 15 and 16 of subsection 76 (12), expressed as a percentage,

“**Q**” is the proportion of “N” that is allocated to the investment categories listed in paragraphs 6 to 11 and 17 of subsection 76 (12), expressed as a percentage, and

“**R**” is the portion of the plan’s target asset allocation for each investment category listed in paragraphs 1, 3 to 11 and 15 to 17 of subsection 76 (12), expressed as a percentage, that is allocated to annuity contracts that have been purchased from an insurance company in respect of benefits.

Content on this page has been transferred from the Financial Services Commission of Ontario (FSCO) site as a PDF for reference. Links that appear as related content have also been transferred and can be found at the end of this document.

The Determination of Whether a Plan is a "Closed Plan"

Revised to reflect the revised definition in Regulation 909 set out in Reg. 105/19

Note: Where this document conflicts with the Financial Services Regulatory Authority of Ontario Act, 2016 (FSRA Act), Pension Benefits Act, R.S.O. 1990, c. P.8 (PBA) or any regulation made under the PBA (Regulations), the FSRA Act, PBA or Regulations govern.

Under Ontario's new funding regime for pension plans that provide defined benefits, whether a plan is closed or not impacts the calculation of a provision for adverse deviations (PfAD) and thus the level of funding required by participating employers.

The definition of a "closed" plan was first introduced on May 1, 2018 under section 11.2(1) of Regulation 909 under the Pension Benefits Act (PBA). Effective May 21, 2019, this definition was amended by Regulation 105/19 as follows:

> "closed plan" means a pension plan:
>
> a. that has no members who are entitled to defined benefits; or
> b. in which at least 25 per cent of the members of the plan who are entitled to defined benefits are in a class or classes of employees from which new members are not permitted, according to the terms of the plan, to join the plan and accrue defined benefits.

Determining if a plan is "closed", requires analysis of the particular facts of that plan. Ultimately, it is the plan administrator who is responsible for making that determination and directing the actuary in that regard. It is important to remember that whether a plan is "closed" or not must be re-determined at every valuation since it is possible that a plan's status may change due to a change of facts since the last valuation.

The Financial Services Regulatory Authority of Ontario (FRSA) does not expect pension plan administrators or their advisors to request FSRA's determination of whether a particular plan is a closed plan; administrators are expected to make and document such a determination, and to obtain any advice they may need to do so. If FSRA has reason to question a statement in an actuarial valuation report to the effect that a plan is not a closed plan, we may ask the signing actuary to provide facts and analysis that support the administrator's determination in this regard.

As a reminder, we note that:

1. while FSRA does not generally indicate its position on whether a plan’s status has or has not been correctly determined in the report filed, this does not mean that FSRA agrees with that determination; and
2. even if FSRA agrees with a determination made by an administrator, that does not mean that the Financial Services Tribunal or a court would necessarily take the same view.

2018 Funding Reform for Defined Benefit Pension Plans

Since the release of the new Ontario funding rules (O. Regulation 250/18) for defined benefit pension plans which came into effect on May 1, 2018, the Financial Services Commission of Ontario (FSCO) has been examining numerous issues related to pension plan funding. In this regard, FSCO has developed communications related to the following:

- **Ability to take contribution holidays and pay PBGF assessments** **UPDATED**
  - Regulation 250/18
  - Updates as a result of Regulation 105/19
- Treatment of excess contributions **UPDATED**
- The determination of whether a plan is a "Closed Plan" **UPDATED**
- Funding and actuarial filing requirements for plan improvements under the new funding regime
- **Frequently asked questions:**
  - Provisions for adverse deviations (PfAD) and funding related disclosures **UPDATED**
  - Annuity purchase and discharge

Ability to Take Contribution Holidays and Pay PBGF Assessments

In response to the new funding regime (set out in section 55.1 of the Pension Benefits Act (PBA) and Regulation 250/18 which amends Regulation 909) that came into effect on May 1, 2018, FSCO has developed a chart illustrating the rules applicable in five scenarios, based on valuation and filing dates. For each scenario, the chart indicates which provisions govern contribution holidays and whether plan surpluses can be used to pay PBGF assessments.

Chart – Ability to take contribution holidays and pay PBGF Assessments Size: ## kb

The chart is based on the following aspects of the new funding regime (unless otherwise indicated, section references are to Regulation 909):

1. Section 55.1 of the PBA came into effect on May 1, 2018 and applies to all pension plans, regardless of the valuation or filing date of the report. Section 55.1 provides that contributions for normal cost (NC) and for the provision for adverse deviations (PfAD) in respect of NC may be reduced or suspended if there is an available actuarial surplus (AAS). AAS is defined under section 7.0.2.
2. The new funding requirements (PfAD & 85% solvency funding threshold) set out in sections 4 and 5 only apply to **a report with a valuation date on and after December 31, 2017 and filed after April 30, 2018**.
3. For reports with **a valuation date on and after December 31, 2017**, section 7(1) does not apply due to section 7(1.1) but the remaining provisions of section 7 (excluding 7(4)) still apply. Therefore, in certain circumstances, plans will be subject to both sections 7 and 7.0.3 and must meet the requirements of both in order to take a contribution holiday.
4. The applicability of section 7.0.3 is premised on the filing date (not the effective date) of a report, i.e., it applies to **a report *filed* on and after December 31, 2017**.
5. The limitations on the amount of actuarial gain that can be applied to reduce NC set out in sections 7(3.1) and 7(3.2) only apply to fiscal years ending before January 1, 2020.
6. The ability to use an actuarial gain to pay a PBGF assessment under section 7(4) was revoked as at May 1, 2018. Therefore, PBGF assessments may be paid under section 7(4) only if they were paid prior to May 1, 2018. Effective May 1, 2018, AAS may be used to pay PBGF assessments in accordance with section 7.0.3(2) – but only where a valuation report has been filed on or after December 31, 2017.

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Ability to take contribution holidays and pay PBGF assessments – revised as per amendments in Regulation 105/19

Revised to reflect the amendments to Regulation 909 set out in Reg. 105/19

Note: Where this document conflicts with the Financial Services Regulatory Authority of Ontario Act, 2016 (FSRA Act), Pension Benefits Act, R.S.O. 1990, c. P.8 (PBA) or any regulation made under the PBA (Regulations), the FSRA Act, PBA or Regulations govern.

In response to the Ontario new funding regime for pension plans that provide defined benefits (set out in section 55.1 of the Pension Benefits Act (PBA) and Regulation 250/18 which amends Regulation 909 (Regulation)) that came into effect on May 1, 2018, the Financial Services Commission of Ontario (FSCO) developed a chart illustrating the rules applicable in five scenarios, based on valuation and filing dates. For each scenario, the Chart indicates which provisions govern contribution holidays and whether plan surpluses can be used to pay Pension Benefits Guarantee Fund (PBGF) assessments.

Ontario Regulation 105/19 (which amends the Regulation) came into effect on May 21, 2019. As a result, scenario 5 of the Chart has been updated. For a valuation report with a valuation date on or after December 31, 2017 and filed on or after May 1, 2018, a contribution holiday can be taken in accordance with the following:

Contribution Holiday Conditions		**Regulation References as amended by Regulation 105/19**
1st plan fiscal year following the date of the valuation *(assuming no off-cycle filing and no filing extension)*	• A valuation report is filed and demonstrates that there is AAS • No need to file actuarial cost certificate within 90 days of the plan fiscal year • PBGF assessment is permitted to be payable from the AAS • If a valuation report is filed more than 6 months after plan fiscal year end, notice of a contribution reduction in the current fiscal year must be given within the	• Maximum AAS as per subsection 7.0.3(4)(a) – subsection 7(3.1.1) clarifies that subsection 7(3.1) does not apply • Subsection 7.0.3(5) applies • Subsection 7.0.3(2) and paragraph 7.0.3(3)(b) apply • Notice timeline per subsection 8(5)

	first 6 months of the next fiscal year	
Subsequent plan fiscal years	• Actuarial cost certificate within 90 days demonstrating that there is AAS • PBGF assessment is permitted to be payable from the AAS • Notice of reduction in contributions must be given within the first 6 months of the fiscal year	• Maximum AAS as per subsection 7.0.3(4) – subsection 7(3.1.1) clarifies that subsection 7(3.1) does not apply • Subsections 7.0.3(2) and (3) apply • AAS at last filed report under section 3 or 14 should be adjusted to reflect any amounts funded from the plan surplus since last valuation date • Notice timeline per subsection 8(4)

For scenarios 1 to 4, the amendments in Regulation 105/19 to the Regulation clarify how each of these scenarios will transition into the ultimate contribution holiday rules outlined above, with the following notes:

a. For fiscal years ending before January 1, 2020, an actuarial cost certificate is still required to be filed within the first 90 days of the fiscal year as per subsection 7(3.1) for scenarios 1 through 4. Section 6.3 exempts plans in these scenarios from the application of section 55.1 under the PBA. Sections 7.0.2 and 7.0.3 are not applicable and there is no requirement to demonstrate the availability of AAS. Useable surplus is limited as per subsection 7(3.2).
b. Despite a) above, and for a fiscal year beginning on or after July 1, 2018, an actuarial cost certificate received beyond the 90-days requirement is acceptable if received on or before June 30, 2019, pursuant to subsection 7(4).
c. A PBGF assessment may be paid from the useable surplus determined under subsection 7(3.2) if the requirements of subsections 7(5) and 7(6) are met.
d. As per subsection 5(16.3), the amount of contributions made prior to the amendments in Regulation 105/19 that would otherwise not have been made if a plan had taken a contribution holiday (assuming it would have been eligible except for PBA section 55.1) can be used to increase the plan's prior year credit balance in the next valuation report if such report has a valuation date on or after December 31, 2017 and is the first report filed on or after May 1, 2018.

Treatment of Excess Contributions

Revised to reflect the amendments to Regulation 909 set out in Reg. 105/19

Note: Where this document conflicts with the Financial Services Regulatory Authority of Ontario Act, 2016 (FSRA Act), Pension Benefits Act, R.S.O. 1990, c. P.8 (PBA) or any regulation made under the PBA (Regulations), the FSRA Act, PBA or Regulations govern.

In response to the Ontario funding rules for pension plans that provide defined benefits which came into effect on May 1, 2018, the Financial Services Commission of Ontario (FSCO) developed and published a communication setting out its positions on the treatment of contributions that have been made by an employer in excess of the required minimum contribution amount set out in the latest filed actuarial valuation report (Communication).

On May 21, 2019, the government amended various provisions of the funding rules in Regulation 909 (Regulation) to come into immediate effect. These include the introduction of a definition of "specified period" under subsection 4(0.1) of the Regulation, as well as new subsections 4(3.2), 4(3.3), 4(3.4), 5(16.3) and section 6.3 of the Regulation. In addition, effective May 29, 2019, section 55.1 of the Pension Benefits Act (PBA) was also amended to add subsection 55.1(4.1). The Financial Services Regulatory Authority of Ontario (FSRA) has updated the Communication to reflect these changes.

"Excess contributions" herein refers to a) any amount paid in excess of the minimum contribution requirements set out in the last filed valuation report, or b) contributions remitted in accordance with the minimum contribution requirement of an expired valuation report until a new valuation report is filed as required by subsection 4(5) of the Regulation that are in excess of the minimum contribution requirements for that period under the new report when filed. In the past, excess contributions have been treated in one or more of the following ways:

1. They formed part of the assets of the fund that get reflected the next time fund assets are measured for actuarial filings, such as valuation reports or cost certificates;
2. They were used to establish a prior year credit balance (PYCB), or increase a PYCB if previously in place, in the next full valuation report;
3. They were used to reduce any contributions otherwise required during the remaining months of the fiscal year in which the new valuation report is filed; or
4. They were returned to the employer pursuant to an application for a refund of an overpayment pursuant to section 62.1(1)(b) of the PBA, provided that the Superintendent of

Financial Services so consented.

FSRA's current positions with respect to "excess contributions" are set out below:

Options	FSRA's Position	Rationale
1) Excess contributions form part of the assets of the fund that get reflected the next time fund assets are measured for actuarial filings, such as valuation reports or cost certificates.	• **This option continues to be available**	• Any excess contributions not applied via options 2 and 3 below remain in the plan fund and then form part of the fund's assets. • The amendments in Reg. 105/19 do not change FSRA's position.
2) Excess contributions are used to establish a PYCB, or increase PYCB if it was previously in place, in the next required actuarial filings.	• **This option continues to be available**. **For listed JSPPs and for plans for which the valuation date is before December 31, 2017 or filed before May 1, 2018:** • From May 1, 2018 to May 20, 2019, a PYCB can be used to reduce contributions for special payments only. Contributions for normal cost (NC) may only be reduced or suspended through the application of available actuarial surplus (AAS). • From May 21, 2019 on, a PYCB can be used to reduce contributions for NC and special payments. **For non-listed JSPPs and plans for which the valuation date is on/after December 31, 2017 and filed on/after May 1, 2018:**	• Section 4(3) of the Regulation permits the employer to apply a PYCB to reduce contributions for NC, PfAD in respect of NC and special payments. However, effective May 1, 2018, section 55.1 of the PBA only permitted a reduction or suspension in the contributions for NC and PfAD in respect of NC from AAS. • Effective May 21, 2019, section 6.3 of the Regulation exempts listed JSPPs and plans that filed valuation reports under the old funding rules from the application of section 55.1 of the PBA. • Section 4(3) of the Regulation permits the employer to apply a PYCB to reduce contributions for NC, PfAD in respect of NC and special payments. However, effective May 1, 2018, section 55.1 of the PBA only permitted a reduction or suspension in the contributions

	• From May 1, 2018 to May 28, 2019, a PYCB can be used to reduce contributions for special payments only. The NC and provision for adverse deviations (PfAD) in respect of NC can only be reduced or suspended through the application of available actuarial surplus (AAS). • Effective May 29, 2019, a PYCB can be used to reduce contributions for NC, PfAD in respect of NC and special payments. • PYCB can be established in a full valuation report under section 14 of the Regulation, a cost certificate as per section 7.1 of the Regulation or a report required under section 3 of the Regulation. • A cost certificate cannot be filed for the sole purpose of establishing or updating a PYCB.	for NC and PfAD in respect of NC from AAS. • Effective May 29, 2019, new subsection 55.1(4.1) of the PBA permits applying a PYCB to also reduce contributions for NC and PfAD in respect of NC, whether or not the plan has an AAS.
3) Excess contributions are used to reduce any contributions otherwise required during the remaining months of the first fiscal year in which the report is filed.	• **This option continues to be available subject to new subsections 4(3.2) and 4(3.3) of the Regulation**.	• New subsection 4(3.2) confirms that excess contributions that were made in respect of the specified period (as defined in subsection 4(0.1) of the Regulation) can be applied to reduce payments otherwise required for the period beginning on the day the report is filed and ending on the earlier of a) the last day of the fiscal year in which the report is filed and b) the filing date of the subsequent report. • It should be noted that in accordance with subsection 4(3.3), subsection 4(3.2) does not apply if the report is filed more than 12 months after the valuation date of the report, even in situations where a

		filing extension has been granted.
4) Excess contributions are returned to the employer pursuant to an application for a refund of an overpayment pursuant to section 62.1(1)(b) of the PBA provided that the Chief Executive Officer consents.	• **This option *is not* available**. • *We note that when FSCO Policy R350-103 was last revised (July 2011), the example of getting a refund in this situation was specifically removed from the policy. In its next iteration, the policy will clearly state that such a situation does not qualify for obtaining a refund under that section.*	• Section 62.1(1)(b) of the PBA addresses refund of an "overpayment"; however, this term is not defined in the PBA or Regulations. • Any so-called "excess contributions" that arise retroactively when a new valuation report is filed, were not actually "excess" at the time they were made, as section 4(5) of the Regulation specifically required those contribution amounts to be made in accordance with report most recently filed at that time. As a result, they are not considered an "overpayment" under section 62.1. • Section 62.1(1)(b) is intended to address payment errors and does not apply to contributions required by section 4(5) of the Regulation or contributions resulting from the decision of an employer or administrator. • The amendments in Reg. 105/19 do not change FSRA's position.

The Determination of Whether a Plan is a "Closed Plan"

Revised to reflect the revised definition in Regulation 909 set out in Reg. 105/19

Note: Where this document conflicts with the Financial Services Regulatory Authority of Ontario Act, 2016 (FSRA Act), Pension Benefits Act, R.S.O. 1990, c. P.8 (PBA) or any regulation made under the PBA (Regulations), the FSRA Act, PBA or Regulations govern.

Under Ontario's new funding regime for pension plans that provide defined benefits, whether a plan is closed or not impacts the calculation of a provision for adverse deviations (PfAD) and thus the level of funding required by participating employers.

The definition of a "closed" plan was first introduced on May 1, 2018 under section 11.2(1) of Regulation 909 under the Pension Benefits Act (PBA). Effective May 21, 2019, this definition was amended by Regulation 105/19 as follows:

> "closed plan" means a pension plan:
>
> a. that has no members who are entitled to defined benefits; or
> b. in which at least 25 per cent of the members of the plan who are entitled to defined benefits are in a class or classes of employees from which new members are not permitted, according to the terms of the plan, to join the plan and accrue defined benefits.

Determining if a plan is "closed", requires analysis of the particular facts of that plan. Ultimately, it is the plan administrator who is responsible for making that determination and directing the actuary in that regard. It is important to remember that whether a plan is "closed" or not must be re-determined at every valuation since it is possible that a plan's status may change due to a change of facts since the last valuation.

The Financial Services Regulatory Authority of Ontario (FRSA) does not expect pension plan administrators or their advisors to request FSRA's determination of whether a particular plan is a closed plan; administrators are expected to make and document such a determination, and to obtain any advice they may need to do so. If FSRA has reason to question a statement in an actuarial valuation report to the effect that a plan is not a closed plan, we may ask the signing actuary to provide facts and analysis that support the administrator's determination in this regard.

As a reminder, we note that:

1. while FSRA does not generally indicate its position on whether a plan’s status has or has not been correctly determined in the report filed, this does not mean that FSRA agrees with that determination; and
2. even if FSRA agrees with a determination made by an administrator, that does not mean that the Financial Services Tribunal or a court would necessarily take the same view.

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Funding and Actuarial Filing Requirements For Plan Improvements under the New Funding Regime

1. Section 3 of Regulation 909 ("Regulation") requires the plan administrator to file a report when a plan amendment changes contributions or creates or changes a going-concern unfunded liability or solvency deficiency. The report must contain any of the information required under section 14 of the Regulation that might be affected by the amendment.
2. The new funding rules and void benefit improvement amendment rule, which came into effect on May 1, 2018, necessitate a review of section 3 report filing requirements. A section 3 report with a valuation date on or after December 31, 2017 (and filed after April 30, 2018) results in the application of the new funding rules to the pension plan.
3. A section 3 report could be in the form of a complete valuation report. A section 3 report prepared this way may be filed under **both** section 3 and section 14.
4. A section 3 report could also only consider the incremental impact of the amendment. However, this option will not be available for the first section 3 report filed after April 30, 2018 if the last section 14 report is filed under the old funding regime. Given that the section 3 report triggers the application of the new funding requirements, all of the information required in a report under section 14 would be affected by the amendment and, therefore, a full valuation must be set out in the section 3 report. In other words in this situation, FSCO will require a section 3 report that contains all of the information that is required in a section 14 report.
5. FSCO Policy A400-100 provided guidance to practitioners regarding FSCO's requirements and expectations under an actuarial cost certificate approach to a section 3 report filing under the old funding regime. Policy A400-100 does not require the filing of a section 3 report if certain conditions are met. Given the new funding regime, this option is no longer available; i.e., where there is a plan amendment that has an effect on funding as set out in section 3 of the Regulation, the actuary must file either a section 3 incremental report (if the last filed report is under the new funding regime) or a complete valuation report which may also be filed as a new section 14 report. Policy A400-100 is currently under review and will be updated.
6. The solvency ratio ("SR") and going-concern funded ratio ("GC Ratio") tests under section 3.0.1(1) or (2) of the Regulation are for the sole purpose of testing if the amendment is void or not under section 14.0.1 of the Pension Benefits Act ("PBA"); they have no funding implication (except for any upfront contributions that the plan sponsor makes to satisfy the requirements under section 3.0.1(1) or (2) of the Regulation).
7. The threshold tests under section 14.0.1 of the PBA are measured as at the later of the effective date of the benefit improvement as stated in the amendment and the date on which the amendment is adopted (generally the Board approval date). The additional contributions to meet the requirements under section 3.0.1(1) or (2) of the Regulation, if any, must be made before the section 3 report is filed in accordance with the timing requirements in section 3(2) of the Regulation.
8. Table A describes how the **incremental funding** is determined under a section 3 report filing (once a prior section 14 report is filed under the new regime). **Generally, funding requirements per the last section 14 report (and any subsequent section 3 reports) previously filed with FSCO remain unchanged except as otherwise noted in Table A**. We have assumed that the thresholds required under section 3.0.1(1) of the Regulation are met (and any upfront contributions as may be required in order to satisfy such thresholds have been made) or that the threshold requirements do not apply due to section 3.0.1(4) or (5).

9. If the thresholds under section 3.0.1(2) of the Regulation are met (instead of the thresholds under section 3.0.1(1) of the Regulation), then the incremental going concern liability and incremental solvency liability will be fully funded. In this situation, only the incremental normal cost (and the associated PfAD) are left to be funded per Table A. Note that section 3.0.1(2) of the Regulation does not require the funding of a PfAD for the increase in going concern liabilities due to a plan amendment.
10. The valuation date for the purpose of a section 3 report (prepared either in an incremental funding or full valuation approach), is the later of the effective date of the benefit improvement as stated in the amendment and the date on which the amendment is adopted. The section 3 report must be filed in accordance with the timing requirement in section 3(2) of the Regulation.
11. This document does not address a situation where the amendment's effective date is after the section 3 report is filed.

TABLE A: Incremental Funding Requirements and Conditions

Funding = Sum of:	Incremental Funding Requirements(a)	Conditions for Reduction in Funding Requirements
Incremental Normal Cost ("NC") and the associated PfAD	• Incremental NC and its associated PfAD (**reflecting PfAD in last valuation filed with FSCO**).	• If the plan sponsor wants to apply available actuarial surplus to reduce the funding of the Incremental NC and its associated PfAD, it can do so by following the rules for a contribution holiday under the PBA and the Regulation(b).
Incremental Going-concern ("GC") Liability	• 8 year amortization of Incremental GC Liability (**no PfAD application**) in excess of any upfront contributions (to get over the thresholds under section 3.0.1(1) of the Regulation), commencing immediately from the valuation date.	• If the plan sponsor wants to apply some or all GC surplus to offset the funding of the Incremental GC Liability (in excess of any upfront contributions), FSCO expects the following conditions to be satisfied: i. Prior to the plan amendment, the plan sponsor is not required to make any GC or solvency special payments; and ii. The actuary can demonstrate that the plan has a GC surplus immediately before any top up contributions (for this purpose, an **updated PfAD** and asset data as at the valuation date must be used). • As a result, FSCO expects the Incremental GC Liability to be offset

		by (i) any upfront contributions (to get over the thresholds under section 3.0.1(1) of the Regulation or otherwise made in respect of the amendment) and (ii) the lesser of the GC surplus as at the last filed report(c) and the updated GC surplus (established above); the resulting amount must be amortized over no more than 8 years. • If the actuary believes that the funded position of the plan has improved, the plan administrator always has the option of filing a section 3 report in the form of a complete valuation report (which may also be filed as a section 14 report).
Incremental Solvency Liability	• 5 year amortization of 85% of Incremental Solvency Liability reduced by any upfront contributions (to get over the thresholds under section 3.0.1(1) of the Regulation) and the present value of any special payments in relation to the Incremental GC Liability established above for the same period, commencing no later than 12 months from the valuation date.	• If the plan sponsor wants to eliminate the funding requirement with respect to the Incremental Solvency Liability, then FSCO expects the following conditions to be satisfied: i. Prior to the plan amendment, the plan sponsor is not required to make any GC or solvency special payments; and ii. The actuary can demonstrate that the plan does not have a reduced solvency deficiency immediately after the plan amendment by using updated asset and market data. • If the actuary believes that there is no reduced solvency deficiency as at the valuation date, after taking the plan amendment into account, the plan administrator always has the option of filing a section 3 report in the form of a complete valuation report (which also may be filed as a section 14 report) in order to avoid solvency special payments.

Notes

a. Under this approach, all funding requirements per the last section 14 report (and any subsequent section 3 reports) remain unchanged; there is not a wholesale re-measurement. Additional contributions are being made to the plan and there is no usage (not even partial usage) of existing assets of the plan to satisfy any funding requirements or increases in liabilities.

   For the purpose of a section 3 report prepared under the incremental funding approach, the valuation methods for both liabilities and assets should be consistent with the last filed section 14 report.
b. Example:
   - Last filed section 14 report at January 1, 2019, indicates Available Actuarial Surplus ("AAS").
   - Plan's fiscal year ending December 31.
   - Actuary files a cost certificate under section 7.0.3(3)(a) of the Regulation for a contribution holiday for 2020.
   - The Board approves the amendment on July 1, 2020, and the effective date of plan amendment is August 1, 2020.
   - Scenario 1
     - A section 3 incremental funding report for the plan amendment is filed on September 30, 2020 indicating no AAS.
     - Contribution holiday ceases, that is, contributions should resume once a section 3 report for the plan amendment is filed and catch-up contributions for the months of August and September, 2020 with interest are also required.
   - Scenario 2
     - A section 3 incremental funding report for the plan amendment is filed on September 30, 2020 with an updated AAS which is greater than the normal cost and its PfAD after the plan improvement for the remainder of the fiscal year.
     - Contribution holiday continues to the end of the fiscal year.
c. The GC surplus as at the last filed report shall be adjusted to reflect any amounts funded from the GC surplus since the date of the last valuation.

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Frequently Asked Questions Pertaining to the 2018 Funding Reform for Defined Benefit Pension Plans

Revised to reflect changes in Reg. 105/19 (in effect on May 21, 2019)

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Frequently Asked Questions Pertaining to the 2018 & 2019 Funding Reform for Defined Benefit Pension Plans

On May 1, 2018, a new funding regime (O. Regulation 250/18) came into effect for pension plans that provide defined benefits. The new regime included a change to the solvency funding rules and the introduction of a new funding provision for adverse deviations (PfAD). The 2018 regime also introduced a new disclosure requirement for the statement of investment policies and procedures (SIPP), set out in sections 78(7) and (8) of the Regulation 909 (Regulation).

After the release of the 2018 funding regime, the Financial Services Commission of Ontario (FSCO) developed frequently asked questions (FAQs) and other communication materials to address questions concerning the new funding requirements. These can be found on the general 2018 Funding Reform for Defined Benefit Pension Plans page.

On May 21, 2019, the government filed O. Regulation 105/19 to amend various provisions of the 2018 funding regime, with immediate effect. Among the amendments were a revised "closed plan" definition for purposes of the PfAD calculation, new provisions relating to excess contributions, changes to the determination of prior year credit balance, clarifying rules for contribution holidays and clarification of the treatment of an investment allocation to bonds that does not meet the minimum credit rating.

The Financial Services Regulatory Authority of Ontario (FSRA) has now updated these FAQs and other communication materials to reflect the changes in Regulation 105/19 . Updated communications can be found here [insert link].

The FAQs are organized as follows:

Provision for Adverse Deviations (PfAD)	
SIPP Content Provision	100 series
Actuarial Issues	200 series
Investment Classification	300 series
Transition Rules	400 series
Funding Related Disclosures	500 series

Provision for Adverse Deviation (PfAD)

The PfAD is prescribed in section 11.2 of the Regulation and provides for an additional level of funding on top of existing normal cost and going concern funding requirements. The PfAD is based on a number of factors, including the asset allocation of the plan, the discount rate, and whether a significant portion of the plan is closed to new members

SIPP Content Provisions

Revised **Q100. What are the new requirements under sections 78(7) and (8) of Regulation 909 and what steps must I take to comply?**

A100. Section 78(7) requires that the SIPP for a plan (other than a jointly sponsored pension plan listed in section 1.3.1(3) of the Regulation or a specified Ontario multi-employer pension plan as provided in section 6.0.4(2.0.1) of the Regulation) include the plan's target asset allocation for assets in respect of defined benefits for each investment category listed in section 76(12) of the Regulation. Section 78(8) describes the target asset allocation for an investment category as the target proportion of the plan's assets invested in a particular investment category in proportion to the total target investment in all investment categories, expressed as a percentage.

To comply with this requirement, the administrator can either amend the existing target asset allocation in the SIPP to reflect the investment categories in section 76(12), or create a second asset allocation table that provides the required target asset allocations.

Where a separate table is established to comply with sections 78(7) and (8), the plan’s actual asset allocation is governed by both the original description of the target asset allocation already found in the SIPP and the description of the target asset allocation in the separate table.

FSRA recognizes that it may take time for the administrator to review and amend the SIPP to meet the requirements of sections 78(7) and (8). FSRA expects the administrator to bring the SIPP into compliance with these sections as soon as is practical, but no later than December 31, 2019. We note that an amendment to a SIPP must be filed with FSRA within 60 days after the date the amendment is made, pursuant to section 78(6) of the Regulation.

In any event, the plan’s SIPP must contain the required asset allocation information on or before the valuation date of a report that calculates the PfAD based on that information.

Q101. Do the new SIPP requirements in sections 78(7) and (8) of the Regulation require every investment category in section 76(12) of the Regulation to be listed in the SIPP, even if there are no investments in that category?

A101. For purposes of sections 78(7) and (8), a SIPP does not need to explicitly list an allocation to an investment category in which the plan does not invest. Investment categories will be deemed to have no allocation if not mentioned in the SIPP.

Revised **Q102. Is it acceptable for the target asset allocation to be listed as a range? Is there any restriction on the ranges that can be specified in a SIPP?**

A102. Under section 11.2(8) of the Regulation, the PfAD is to be based on the target asset allocation as documented in the plan’s SIPP, and requires a single figure expressed as a percentage for each section 76(12) (of the Regulation) investment category in which the plan invests. A range would not work for purposes of the PfAD calculation, but can be included in the SIPP in addition to the target (as is commonly done).

The SIPP should identify any portion of the target asset allocation into categories 4, 15 and 16 that are not required to meet the minimum credit rating for the applicable investment category.

With respect to the second part of this question, there is no specific restriction on the asset allocation ranges that can be specified in the SIPP. However, an overly wide asset allocation range may not provide necessary investment control and monitoring of that asset category.

We also make note of the *Guideline for the Development of Investment Policies and Procedures for Federally Regulated Pension Plans*, published by the Office of Superintendent of Financial Institution, which provides useful guidance on developing investment policy, and advises that the range of possible allocations should be sufficiently narrow so that:

- the intentions of the administrator are clear;
- the activities of investment managers can be controlled; and
- third parties can assess the security of benefits.

Revised **Q103. Section 78(7) of the Regulation requires the SIPP to state the plan's target asset allocation for assets in respect of defined benefits for each investment category in section 76(12) of the Regulation. For plans that invest entirely in pooled funds, how would the requirement in section 78(7) be applied?**

A103. FSRA recognizes that a pooled fund is an investment vehicle, and not strictly speaking an asset class. There are two acceptable approaches to addressing pooled funds in the target asset allocation in the SIPP.

Under the first approach, the SIPP does not have to specify an allocation to pooled funds (investment category 2), even if the plan ultimately employs these vehicles. The SIPP can instead set out its target asset allocations using the other investment categories listed in section 76(12). In doing so, the administrator is indicating that it does not allocate any assets to pooled funds as an asset class, although it may use pooled funds to achieve its allocation to the investment categories that are indicated.

Under the second approach, the administrator may decide to indicate that it has allocated all (or a stated portion) of its assets to the "pooled fund" investment category. If it takes this approach, then the SIPP must also indicate what the underlying allocation is to the various investment categories listed in section 76(12) in order to permit the calculation of the PfAD in accordance with the look-through rules set out in section 11.2(8) of the Regulation. (The definitions of "N", "P" and "Q" in section 11.2(8) require the administrator to "look through" assets invested in pooled funds, and determine the proportion of those assets that are invested in investment categories "L" and "M", as defined in section 11.2(8)).

Where applicable, the SIPP should specify that the fund is permitted (or required) to invest plan assets using pooled funds.

Revised **Q104. Section 11.2(10) of the Regulation requires the use of the target asset allocation in the SIPP that "is in effect as of the valuation date". What does this mean?**

A104. A SIPP is normally "in effect" either on the date it is approved or the date it is amended by the administrator. Where a SIPP specifically states a future effective date, the previous SIPP would still be considered to be "in effect" until that future date. For the purpose of determining the PfAD, the target asset allocation in the SIPP in effect as of the valuation date must be used and referenced. Future changes to the asset allocation noted in the SIPP, such as those in a de-risking glide path, that would occur after the valuation date of the report are not to be considered in calculating the PfAD. This differs from the practice of setting the discount rate for purposes of the valuation report. In that case, the actuary needs to exercise professional judgement in reflecting any pending changes to the plan's investments.

Actuarial Issues

Q200. For plans that have an explicit normal cost for expenses, should the PfAD be applied to this portion of the normal cost?

A200. For the purpose of the going concern valuation, the PfAD should be applied to any provisions for plan expenses payable from the pension fund.

Q201. Does the new PfAD satisfy any margin requirement in the going concern discount rate noted in section 1 of Actuarial Guidance Note AGN-001?

A201. Effective May 1, 2018, the PfAD is a legislated additional funding target requirement under the Regulation. In preparing a going concern actuarial valuation, the actuary needs to exercise professional judgement to determine whether an additional margin for conservatism is warranted; this includes, but is not limited to, taking into account the terms of engagement and relevant funding policy of the pension plan. For example, consideration should be given to whether there is a need or desire to build a funding buffer via additional margin for conservatism to enable plan stakeholders to better manage the volatility of funding obligations or sustainability of the plan's benefits in a going concern context. Also, the actuary is expected to provide a rationale in the valuation report for any changes in assumptions, including any changes in margins. FSRA will undertake a review of our Actuarial Guidance Notes and revise as appropriate to reflect the requirements of the new funding regime.

Revised **Q202. When is a plan considered to be a "closed plan" for purposes of section 11.2 of the Regulation?**

A202. Effective May 21, 2019, the definition of a "closed plan" has been revised and is defined in section 11.2(1) of the Regulation as follows:

"closed plan" means a pension plan:

a. that has no members who are entitled to defined benefits; or
b. in which at least 25 per cent of the members of the plan who are entitled to defined benefits are in a class or classes of employees from which new members are not permitted, according to the terms of the plan, to join the plan and accrue defined benefits.

Determining if a plan is "closed" requires analysis of the particular facts of that plan. Ultimately, the administrator is responsible for making that determination and directing the actuary in that regard. It is important to remember that whether a plan is "closed" or not must be re-determined at every valuation since it is possible that a plan's status may change due to a change of facts since the last valuation.

For more information, refer to the revised position paper *The determination of whether a plan is a "Closed Plan"*.

Investment Classification

The questions below address the classification of certain investments for the purposes of calculating the PfAD. FSRA expects that the administrator, in consultation with its agent(s), will determine the appropriate classification of the investment or asset class. Both the administrator and, where applicable, its agent(s) should be prepared to justify any classification.

Revised **Q300. How would an investment in a real estate investment trust (REIT) be classified for purposes of determining the PfAD?**

A300. The classification of an investment in a REIT will depend on the nature of the investment. For example, an interest in a REIT which is held through shares in a corporation would be classified as the investment category described in either paragraph 13 or 14 of section 76(12) of the Regulation, depending on whether it is a domestic or foreign corporation, and assuming none of the investment categories in paragraphs 1 to 12 apply. However, an interest in a REIT which is held through some other legal structure, such as a partnership or trust agreement, would be classified as the investment category described in paragraph 17 (assuming none of the categories in paragraphs 1 to 16 of section 76(12) apply). As an investment in a REIT is not a direct investment in real estate, it would not be classified as the investment category described in paragraph 7.

Revised **Q301. What is a real estate debenture as referred to in paragraph 8 of section 76(12) of the Regulation?**

A301. For purposes of section 76(12), “real estate debenture” can be defined as a debt obligation backed by the credit of the real estate property owner, and not by the collateral of the real estate property itself. A real estate debenture is classified as an “M” item for purposes of determining the combined target asset allocation for fixed income assets under section 11.2(8) of the Regulation.

Revised **Q302. Is private equity a “stock” and hence a non-fixed income asset under the PfAD rules, or is it not a stock, and hence falls under the investment category under paragraph 17 of section 76(12) of the Regulation and categorized as “M” for purposes of determining the combined target asset allocation for fixed income assets under section 11.2(8) of the Regulation?**

A302. The classification of a private equity investment will depend on the nature of the investment. For example, private equity that is accurately characterized as venture capital should be classified as the investment category described in paragraph 10 (venture capital) of section 76(12). Private equity that is in the form of Canadian or foreign “stock” (and is not venture capital) should be classified as the category of investment described in either paragraph 13 or 14 (Canadian or foreign stocks), depending on whether it is a domestic or foreign corporation and assuming none of the investment categories in paragraphs 1 to 12 of section 76(12) apply.

Revised **Q303. What is meant by the term "insured contracts" in paragraph 1 of section 76(12) of the Regulation and the term “benefits for which an annuity contract has been purchased from an insurance company” as used in sections 11.1 and 11.2 of the Regulation?**

A303. It is FSRA’s view that both of these terms refer to buy-in annuities and buy-out annuities that are not subject to a discharge under section 43.1 of the PBA.

Buy-out annuities that are subject to a discharge under section 43.1 of the PBA, however, should no longer be included in the assets or liabilities of the plan, and therefore would not need to be included in the PfAD calculations.

Revised **Q304. How should infrastructure investments be treated under the PfAD rules?**

A304. The classification of an investment in infrastructure will depend on the nature of the investment. For example, an investment in the shares of a Canadian infrastructure enterprise would be classified as the category of investment described in either paragraph 13 or 14 (Canadian or foreign stocks) of section 76(12) of the Regulation, depending on whether it is a domestic or foreign corporation, and assuming none of the categories in paragraphs 1 to 12 of section 76(12) apply. However, an interest in infrastructure which is held through some other legal structure, such as a partnership or joint venture, would be classified as the investment category described in paragraph 17, assuming none of the categories in paragraphs 1 to 16 of section 76(12) apply.

Q305. How are commodities treated under the PfAD rules?

Revised **A305.** The classification of an investment in commodities will depend on the nature of the investment. For example, the purchase of actual gold, or of gold futures, would be classified as the investment category described in paragraph 17 (other investments) of section 76(12) of the Regulation. Alternatively, the investment may take the form of an investment in the shares of a company that produces the commodity (e.g., mining company), in which case the investment would be classified as the investment category described in either paragraph 13 or 14 (Canadian or foreign stocks), depending on whether it is a domestic or foreign corporation, and assuming none of the categories in paragraphs 1 to 12 of section 76(12) applies.

Q306. Derivatives and leverage strategies can have an impact on the overall return/risk profile for the pension fund. However, the methodology for calculating the PfAD does not explicitly address their use. Are derivatives and leverage strategies to be considered in the PfAD calculations, and if so, how?

A306. Under sections 11.2(9) and (10) of the Regulation, the PfAD is calculated using the plan’s target asset allocation as set out in the plan’s SIPP. Accordingly, the treatment of derivatives and leverage strategy will depend on how they are reflected in the target asset allocation, if at all.

Revised **Q307. If a bond held by a pension fund does not meet the minimum credit rating requirements, how is it treated under the PfAD rules?**

A307. Under sections 11.2(9) to (10) of the Regulation, the determination of the level of fixed income assets is not affected by any specific bond that is actually held in the portfolio. Instead, it depends on the target asset allocations (or the portion thereof), as set out in the SIPP, to the investment categories described in paragraphs 15 and 16 (Canadian bonds and Foreign bonds) of section 76(12) of the Regulation, that meets the minimum rating for such category (as set out in the tables under section 11.2) given by a credit rating agency recognized by a competent authority. Any portion of a target allocation for an investment category listed in paragraph 15 or 16 of section 76(12) that is not required to meet the minimum credit rating will be in a 50% fixed income category (i.e., included in "M" or "Q").

Revised **Q308. How is private debt treated under the PfAD rules?**

A308. Private debt would fall into the investment category described in either paragraph 15 or 16 (Canadian or non-Canadian bonds and debentures) of section 76(12) of the Regulation, assuming that none of the categories in paragraphs 1 to 12 of section 76(12) apply, but its treatment is subject to the credit rating requirement in section 11.2(9) of the Regulation.

A target asset allocation in a plan's SIPP for the investment category described in either paragraph 15 or 16, or a portion thereof, is only considered to be fully fixed income if the allocation, or portion thereof, meets the minimum rating for investments in that category (as set out in the tables under section 11.2) given by a credit rating agency recognized by a competent authority. Any portion of a target asset allocation for an investment category listed in paragraph 15 or 16 of section 76(12) that is not required to meet the minimum credit rating will be in a 50% fixed income category (i.e., included in "M" or "Q").

Q309. What is meant by a "competent authority" in the phrase "by another credit rating agency recognized by a competent authority" as set out in sections 11.2(9) and (12) of the Regulation?

A309. We understand that "competent authority" generally refers to a financial regulatory or supervisory authority recognized by legislation.

Q310. For private debt, can an internally-developed credit rating from a third party investment manager be considered sufficient for the purpose of section 11.2(9) and

(12) of the Regulation?

A310. No.

New **Q311. If an investment-grade bond was downgraded below the minimum credit rating as set out in the SIPP, would this impact the calculation of a PfAD?**

A311. The calculation of a PfAD is based on the target asset allocation set out in the plan's SIPP. As a result, the downgrading of a bond that is actually held by the plan would not affect the calculation of a PfAD. However, the administrator may have to dispose of the bond within a reasonable period of time, in order to remain in compliance with its SIPP.

Transition Rules

The following questions address the transition rules relating to component B of the PfAD formula, as prescribed under sections 11.2(11) and (12) of the Regulation. These transition rules may be applied to valuation reports with a valuation date before December 31, 2019.

Q400. How do the transition rules work under sections 11.2(11) and (12) of the Regulation?

A400. Under the transition rules, a plan's actual asset allocations to the section 76(12) (of the Regulation) investment categories on the valuation date of the report, as set out in the plan's financial statements, may be used instead of the plan's target asset allocations in determining the values of "L", "M", "N", "P", "Q" and "R" in section 11.2(8) of the Regulation.

The transition rules may be used to calculate the PfAD in a valuation report with a valuation date before December 31, 2019.

Revised **Q401. Under the transition rules, how is a bond that does not meet the minimum credit rating requirements set out in section 11.2(12) of the Regulation treated? Does it impact other investment grade bonds in the same investment category?**

A401. The bond would be classified as the investment category described in paragraph 15 or 16 (Canadian or foreign bonds and debentures) of section 76(12) of the Regulation, depending on whether it is issued by a Canadian or foreign company. For purposes of the PfAD calculation, the bond would be classified as “M’ (i.e., treated as 50% fixed income). The bond would not adversely affect the classification of other investment-grade bonds held in the same investment category.

Revised **Q402. If a pooled fund has a small target allocation to high yield bonds (which would not meet the minimum credit rating referred to in section 11.2 of the Regulation), how is the pooled fund treated for purposes of the PfAD under the transition rules?**

A402. The definitions of “N”, “P” and “Q” in section 11.2(8) of the Regulation require the administrator to “look-through” assets invested in pooled funds, and determine the proportion of those assets that are invested in investment categories “L” and “M”, as defined in section 11.2(8).

Where the PfAD is calculated based on the actual asset allocation under the transition rules, the administrator, in consultation with its agent(s), can classify bonds individually.

Under this approach, if a pooled fund had 85% invested in investment grade bonds which meet the credit rating described in the Regulation, and 15% high yield bonds that do not meet the credit rating, for purposes of calculating the PfAD, the actual bonds held in the pooled fund that meet the credit rating (i.e., 85%) would be treated as fixed income assets (i.e., included in “P”), and the bonds that do not meet the credit rating (i.e., 15%) would be treated as 50% fixed income assets (i.e., included in “Q”).

Revised **Q403. How is private debt treated under the transition rules?**

A403. Under the transition rules, an investment in private debt that does not meet the minimum credit rating requirements in section 11.2(12) of the Regulation would not be considered a 100% fixed income asset, and would be classified as an “M” investment (i.e., 50% fixed income asset). However, the private debt investment would not adversely affect the classification of other investment grade bonds held in the same investment category.

Q404. How are derivatives and leverage strategies considered in the PfAD, under the transition rules?

A404. Under the transition rules, the PfAD is calculated using the plan's actual asset allocation as set out in the plan's financial statements. Accordingly, the treatment of derivatives or a leverage strategy will depend on how they are reflected in the actual asset allocation in the financial statements, if at all.

Funding Related Disclosures

Revised **Q500. In any plan year where the employer is taking a contribution holiday, is the plan administrator required to notify the plan membership?**

A500. Yes, the plan administrator is required to notify the plan membership of a contribution holiday and this notice must be given to plan members, former members, retired members, trade unions and the plan advisory committee, if any. The timing for providing this notice, however, depends on when the contribution holiday occurs. In general, notice about a contribution holiday must be given within the first six months of the fiscal year in which the contribution holiday is taken as required in section 8(4) of the Regulation. However, if a contribution holiday is commenced during the first year following the valuation date of a newly-filed report but more than six months after the start of that fiscal year, notice with respect to the contribution holiday taken in that fiscal year must be given within the first six months of the next fiscal year, as required under section 8(5) of the Regulation.

It should be noted that a separate notice to a member, former member or retired member is not required if the administrator includes the information required under section 8(3) of the Regulation in the annual or biennial statement provided to such member, former member or retired member in the same fiscal year.

Q501. Is section 4(1.3) of the Regulation only applicable to a report filed under the new rules?

A501. No. Section 4(1.3) provides that any amendment that is required for purposes of complying with section 4(1.1) of the Regulation shall be made within 12 months after the date the first report with a valuation date on or after December 31, 2017, is filed. The Regulation does not make a distinction as to whether the report was prepared under the old or new funding rules.

Q502. Under the new funding regime, new sections 40(1)(p)(v.1), 40.1(1)(m)(i.1) and 40.2(1)(l)(i.1) of the Regulation were added to the disclosure requirements and come into effect on January 1, 2019. What does this mean for plan administrators issuing statements to the plan membership on and after this date?

A502. The new disclosure provisions require the disclosure of the plan's estimated transfer ratio as at the end of the statement period. These provisions came into effect on January 1, 2019. This means that plan administrators must comply with these new disclosure requirements in statements (whether annual or biennial) issued on and after January 1, 2019.