

# Approach



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## Limitations on Commuted Value Transfers and Annuity Purchases (DB Pension Plans)

### Purpose and Scope

This Guidance outlines FSRA’s Approach<sup>1</sup> to reviewing applications to transfer commuted values (“CVs”) or to purchase annuities pursuant to sections 19(4) and (5) of Regulation 909 (the “Regulation”) under the *Pension Benefits Act* (the “PBA”) – and to how FSRA<sup>2</sup> will exercise its discretion in those matters. This Approach guidance has been developed to address events when a defined benefit pension plan’s transfer ratio (“TR”) has declined by ten per cent (10%) or more and the resulting TR is below 0.9; it replaces FSCO Policy T800-402, *Commuted Value Transfers*, which became effective July 7, 2009, until further notice.

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<sup>1</sup> Approach Guidance is one of the four types of guidance that may be issued under FSRA’s [Guidance Framework](#). Approach Guidance describes FSRA’s internal principles, processes and practices for supervisory action and application of CEO discretion. Approach Guidance does not create compliance obligations for regulated parties but can be considered indicative of FSRA’s position and does not alter the requirement to comply with the existing legal and regulatory framework.

<sup>2</sup> Pursuant to Section 19(4) and (5) of the Regulation, the transfer of a CV entitlement is subject to the approval of the Chief Executive Officer. However, for the purposes of this Approach Guidance, the reference will be to FSRA.

## Rationale and Background

Beneficiaries whose employment has terminated (or in some cases, their spouse or beneficiaries) are entitled to transfer the CV of their entitlement out of the pension plan.<sup>3</sup> As well, administrators may purchase annuities to discharge pension liabilities under the pension plan.<sup>4</sup>

Where conditions triggering the application of sections 19(4) and (5) of the Regulation have not occurred, full CV transfers and annuity purchases may proceed if the pension plan's TR (as reported in the last filed valuation report) is greater than or equal to 1.0. Otherwise, if the pension plan's TR is less than 1.0, then the pension plan can only transfer the portion of the CV equal to the CV multiplied by the TR reported in the last filed valuation report unless:

- the administrator is satisfied that an amount equal to transfer deficiency has been remitted to the pension fund; or
- the aggregate of all transfer deficiencies for all transfers made since the effective date of the last filed valuation report is less than five per cent (5%) of plan assets.<sup>5</sup>

However, any deficiency that is not initially transferred out, must be transferred in no more than five years.<sup>6</sup>

### **Conditions Triggering Application of Sections 19(4) and (5)**

If the administrator "*knows or ought to know*" that, since the date of the most recently filed valuation report, events have taken place that result in a reduction in the TR:

1. to less than 0.9 when the TR was  $\geq 1.0$ ; or
2. of at least 10% when the TR was less than 1.0;

then all CV transfers, and Section 43 of the PBA annuity purchases, are automatically suspended.<sup>7</sup> In these circumstances, administrators may choose to apply to FSRA for approval to continue CV transfers and / or annuity purchases.

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<sup>3</sup> Transfers made pursuant to Sections 42 and 48 of the PBA.

<sup>4</sup> Annuities purchased pursuant to Section 43 of the PBA.

<sup>5</sup> Section 19(6) of the Regulation.

<sup>6</sup> Sections 19(7), (7.1) and (7.2).

<sup>7</sup> Section 19(4) and (5) of the Regulation.

Also, when 19(4) or (5) of the Regulation apply, the provisions of sections 19(6), (7), (7.1) and (7.2) do not automatically apply. However, FSRA's approvals may set out similar requirements.

During periods of market uncertainty, administrators should be ready to determine if section 19(4) or (5) of the Regulation apply at any time – administrators cannot rely solely on carrying out quarterly checks of the TR.

## Principles

FSRA's statutory objects, as outlined in the *Financial Services Regulatory Authority of Ontario Act, 2016* (FSRA Act), include to promote good administration of pension plans and to protect and safeguard the pension benefits and rights of pension plan beneficiaries.<sup>8</sup>

When events take place that negatively impact the TR of a plan (as defined under sections 19(4) and 19(5) of the Regulation), FSRA will, in its review of applications, assess risks posed to plan beneficiaries – terminating and remaining plan beneficiaries – with an aim to ensure that pension promises can be delivered over the long-term. This may include, amongst other things:

- the potential for inequity that may arise if some beneficiaries receive full CV transfers and the remaining beneficiaries face a heightened possibility of receiving less than their full CVs in the future;
- the pension plan's risks, ability to absorb further shocks, impact of the current funding and investment strategy, and projected funded status of the plan over the next five years;
- the sustainability of the pension plan in relation to the financial stability of participating employers; and
- the ability to reduce benefits retroactively under the pension plan.

FSRA will strive to be reasonable and risk-based, minimizing unnecessary disruption of CV transfers and annuity purchases, while appropriately protecting entitlements of plan beneficiaries.

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<sup>8</sup> FSRA Act section 3.

We recognize that administrators and other plan fiduciaries are responsible for prudently managing risks in their pension plans, ensuring the long-term financial sustainability of those plans, and making decisions taking into account the interests of all beneficiaries (meaning, those requesting CVs and those who continue to retain entitlements in the pension plan).

## Processes and Practices

When FSRA reviews an application to continue CV transfers, we will consider an expedited review process for those that qualify, as described below. For all other applications to continue CV transfers, there will be a more in-depth review process which will require more time.

Administrators should consider the situation as soon as practicable after becoming aware that section 19(4) or (5) of the Regulation has been triggered. Administrators need to assess, in their fiduciary capacity, whether it is in the best interests of all plan beneficiaries, and the sustainability of the pension plan, to request a continuation of CV transfers, and if so, at what level. The administrator should inform FSRA of its decision and intended plan of action in a timely manner.

A Form 10 is required to be filed if CV transfers are to continue. The applicant does not need to specify an expedited or in depth review process – FSRA will determine the level of review. FSRA may deny approval to any application and has authority to add terms and conditions to its approval and / or request additional information.<sup>9</sup>

FSRA may carry out ongoing supervision of the pension plans it regulates, whether a Form 10 is filed or not, and FSRA may require additional information or reporting while the circumstances leading to the triggering of section 19(4) or (5) of regulation persists. FSRA's prudential supervision will focus, among other things, on balancing the stability of pension plans over time with members' rights.

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<sup>9</sup> Sections 42(7), (8) and (9) of the PBA.

## For CV Transfers:

### 1. No Approval Requested.

As described above, all administrators must cease to transfer CVs when they know or ought to know that the pension plan's TR has dropped as described in section 19(4) or (5) of the Regulation. In some cases, an administrator, after fully considering its obligations under the PBA and its fiduciary obligations to all plan beneficiaries, may decide that the best course of action until plan stability has improved is not to apply for approval to continue CV transfers. The result would be a continued cessation of all CV transfers. Administrators should obtain legal and actuarial advice before making this decision.

FSRA requests that it be notified, in a timely manner, when an administrator adopts this approach. The administrator (or its advisor) should explain the reasons for taking this approach and the factors that were considered (for example, infrequent terminations, liquidity considerations, balancing the interests of all plan beneficiaries, financial conditions of participating employers, etc.). In addition, the administrator should indicate: (i) how long the cessation of CV transfers is expected to continue, (ii) what communication is being made to plan beneficiaries, and (iii) what steps are being taken to return to a situation where CV transfers can be made. FSRA may request additional information.

### 2. Expedited Process

Administrators should review the criteria and considerations below, along with FSRA's principles and the need to balance the interests of all plan beneficiaries in making their Form 10 application. The application will generally be considered under this process if:

- a) the administrator proposes to transfer out full CVs if it is satisfied that an amount equal to the full transfer deficiency (based on the updated TR) has been remitted to the fund by the participating employer with respect to each CV transfer; or
- b) the pension plan's updated TR is at least 0.85 and the administrator proposes to transfer out full CVs, so long as the aggregate of all transfer deficiencies since the last valuation date does not exceed five per cent (5%) of the plan's assets at that time; or
- c) the updated TR is less than 0.85 and the administrator proposes to only transfer out a portion of the CV at the updated TR, with the remainder being transferred out within no more than five (5) years.

- Guided by our statutory objects and the principles outlined in this Approach, FSRA may determine that an application to proceed as described in (b) or (c), above, requires additional review under our in-depth process.
- FSRA may also, at its discretion, allow an expedited process on more lenient terms where warranted after considering the principles outlined in this Approach.
- Under this expedited process, FSRA will strive to respond to applicants within five (5) business days of receiving a completed Form 10. Incomplete applications or applications where FSRA requires additional information to make a well-informed decision to protect the plan and plan beneficiaries may result in delays.

### 3. In-Depth Process

An in-depth review may require that additional information be provided to FSRA. While FSRA will strive to respond to the applicant within fifteen (15) to twenty (20) business days, administrators should expect that this review process may, in some cases, take longer.

Our in-depth review and decision-making regarding applications may take into consideration, amongst other things, any of the following:

- the financial position of the pension plan, including the plan's funded level based on the most recent valuation, the estimated drop in the plan's TR, and an estimate of the plan's funded status at Year 5 from the date of application;
- identification of liquidity concerns (or the lack of any such concerns);
- the expected frequency of terminations and the average size of termination CVs;
- a description of the impact of transfer deficiencies on the plan's assets and TR (i.e., the size of the transfer deficiencies relative to the plan's assets) – and the potential impact of transfers on the benefit security of remaining plan beneficiaries;
- the impact of continued market uncertainty and further events;
- any concern over the specific pension plan's investment portfolio;
- any concern over the employer(s)' ability to absorb fluctuations in plan costs or fund deficiencies on wind up; and

- for multi-employer pension plans (“MEPPs”), existing benefit reduction practices and how they will be applied when there are temporary CV reduction under section 19 of the Regulation.<sup>10</sup>

Administrators are encouraged to include information that addresses any or all of the above possible factors (or any other relevant information) with their Form 10 application.

FSRA’s in-depth review may lead it to deny approval, or to provide approval to transfer 100% of the CV or something less.

## Terms and Conditions

As noted, FSRA has authority to attach terms and conditions to any approval it grants under the expedited process or the in-depth process. The intent of such terms and conditions is to enable FSRA to fulfill its role as a principles-based prudential regulator and its regulatory responsibility to promote good plan administration and safeguard the rights and benefits of pension plan beneficiaries.

Such terms and conditions will often include, but are not limited to, any of the following:

- Imposing a test similar to what is found in section 19(6)(b) of the Regulation, or something more restrictive;
- A requirement to transfer out only a portion of CVs;
- Rules regarding when the requirements / applicability of FSRA’s approval will cease to apply;
- Rules concerning when the remaining portion of a CV can be transferred if less than 100% is initially transferred;
- The identification of any exceptions to the approval being granted;
- A requirement to provide additional or updated information (including a funding plan) in the future;
- A requirement to cease or vary the level of CV transfers in the future; and

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<sup>10</sup> Some MEPPs have plan terms that reduce benefits, resulting in a lower benefit with a lower CV. In that situation, a section 19) reduction in the CV would be applied to the plan-reduced CV. In these cases, MEPPs may wish to request an alternative reduction factor that would be more appropriate given the plan’s rules /practice.

- A requirement to adhere to such additional terms and/or conditions as FSRA may require from time to time.

Any approval given by FSRA remains in effect until the earlier of the date the next valuation report<sup>11</sup> is filed or the date the TR drops by five per cent (5%) or more from the level identified in the most recently filed Form 10 (triggering a new cessation of CV transfers) – or until FSRA revises its previous decision.

## Resumption of Full CV Payments

Administrators that elect not to file a Form 10 are expected to have a plan to allow them to return to a situation where CVs can be transferred. Those administrators can resume making CV transfers if:

- a new, full valuation report is filed pursuant to section 3 or 14 of the Regulation and CVs can be transferred pursuant to the requirements of section 19 of the Regulation;<sup>11</sup> or
- FSRA approval is obtained after filing a Form 10 with an updated TR, determined as at the date the past event under section 19(4) or (5) of the Regulation occurred (i.e., for which the administrator initially did not file a Form 10); or
- at the same time as filing a Form 10 (or later), and if in accordance with FSRA's approval, the administrator also files a statement signed by the plan's actuary (within sixty (60) days of the measurement date), showing an estimated updated TR  $\geq 0.9$ .

Administrators who have filed a Form 10 and have been denied approval by FSRA to transfer CVs or have been approved to transfer CVs at less than one hundred per cent (100%), can resume unreduced CV transfers if:

- a new, full valuation report is filed pursuant to section 3 or 14 of the Regulation and the TR is equal or greater than 1 or the conditions in section 19(6) are satisfied;<sup>11</sup> or
- participating employers fully fund deficiencies with respect to all CV transfers; or
- It is a term of FSRA's prior approval, and a statement signed by the plan's actuary is filed with FSRA (within sixty (60) days of the measurement date of the TR) showing an estimated updated TR  $\geq 0.9$ .

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<sup>11</sup> See Filing a Valuation Subsequent to Filing a Form 10 in the Appendix for more information.

## When the TR Falls by an Additional Five Per Cent (5%) or Greater

Where an administrator knew or ought to have known that a section 19(4) or (5) of the Regulation event has occurred because its plan's TR fell by at least ten per cent (10%) and the resulting TR ratio is below 0.9, and the administrator received approval to transfer CV's on some basis after filing a Form 10, and then, subsequently knows or ought to know that the plan's TR has declined by at least an additional five per cent (5%) from the level identified in the previously filed (and still in effect) Form 10, the administrator must again cease transferring CVs and decide whether to file another Form 10 reflecting the newly updated TR.

## Exceptions

For clarity, FSRA will generally authorize transferring (as a term or condition) CVs in the following circumstances:

- Already existing transfer deficiencies will continue to be subject to any existing terms and conditions established when the deficiency arose.
- Benefits payable under a shortened life expectancy provision<sup>12</sup> will be payable in full.
- Death benefits pursuant to section 48 of the PBA, or the remainder of any guarantee period for a post-retirement death, will be payable in full.

For further clarity, we note that "small benefit" transfers<sup>13</sup> and transfers made pursuant to a reciprocal transfer agreement<sup>14</sup> are exempted from the operation of sections 19(2) to (7) of the Regulation.<sup>15</sup>

## Communicating with Beneficiaries

The administrator must consider its fiduciary obligations when deciding when and what to report to beneficiaries, once the conditions in 19(4) or (5) of the Regulation have been met. This is true whether or not the administrator files a Form 10 or FSRA approval is received. The administrator can decide how best to communicate any information in this regard.

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<sup>12</sup> Section 49(1) or (2).

<sup>13</sup> Sections 44(7) and 50 of the PBA.

<sup>14</sup> As defined in section 1 of the PBA.

<sup>15</sup> Section 19(8) of the Regulation.

Generally, administrators should inform persons entitled to a CV transfer, pursuant to the PBA or plan terms, about any restrictions that apply to the transfer of CVs. Administrators must continue to provide eligible terminating and retiring beneficiaries with option statements containing the information required by the PBA and Regulation within prescribed timelines.<sup>16</sup> Those statements must inform the recipient if all or a portion of the CV must remain in the plan and the time frame within which the remainder is expected to be transferred out.<sup>17</sup>

Administrators must take into account the current situation when considering whether to allow beneficiaries to exercise rights under the plan that are subject to time limits.

### **Transferring any Remaining Portion of a CV**

If FSRA approves the continuation of CV transfers at less than one hundred per cent (100%), then it will generally make it a term of its approval that the remainder must be transferred out within no more than five (5) years. The terms on which the transfer of the remainder will be made will be agreed with FSRA in the approval or otherwise on a case-by-case basis.

### **For Annuity Purchases**

For administrators who wish to purchase annuities<sup>18</sup> pursuant to section 43 of the PBA, if section 19(4) or (5) of the Regulation apply, a Form 10 must be filed and the approval of FSRA must be received. FSRA will generally require employer(s) to contribute the full amount of any deficiency (based on the updated TR) before the purchase can be made.

Annuity purchases made pursuant to section 43.1 of the PBA are not subject to section 19 of the Regulation, but must comply with the requirements of section 43.1 and applicable regulation.

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<sup>16</sup> FSRA understands that during the COVID-19 period some administrators may experience challenges meeting communication timelines and has issued Guidance in that regard.

<sup>17</sup> MEPPs whose terms provide that some or all of such remaining amounts are or may be eliminated and not be paid at all, must inform the recipient of that fact as well.

<sup>18</sup> FSRA considers “*buy-in*” annuities to be a plan investment, where the plan remains primarily responsible for paying and administering the monthly pensions referenced in the buy-in annuity contract. As a result, buy-in annuities are not subject to section 42, 43 or 43.1 of the PBA or section 19 of the Regulation.

## Additional Information

Administrators may attempt to facilitate the review of their application by providing supporting documents and information to FSRA in advance of filing Form 10. Administrators should submit their Form 10 through the [Pension Services Portal](#), or email [PensionInquiries@fsrao.ca](mailto:PensionInquiries@fsrao.ca) if they have questions about completing Form 10.

## Effective Date and Future Review

This Approach Guidance became effective on **(May 22, 2020)** and will be reviewed no later than December 31, 2020. FSRA may withdraw, amend, revise, or extend this Guidance at any time.

## About this Guidance

This Guidance is an Approach. Approach Guidance describes FSRA's internal principles, processes and practices for supervisory action and application of Chief Executive Officer discretion. Approach Guidance may refer to compliance obligations but does not in and of itself create a compliance obligation. Visit [FSRA's Guidance Framework](#) to learn more.

## Appendix

The Request for Approval form (Form 10) is to be signed by the administrator (declaration of the administrator). The Actuarial Certification that accompanies the request for approval must be signed by the plan's actuary and must include:

- the effective date of the updated TR calculation (the "determination date")
- the market value of the plan assets as of the determination date
- the prior year credit balance, if any
- the solvency liabilities of the plan
- the liabilities for benefits, other than pension benefits and ancillary benefits payable under qualifying annuity contracts, that were excluded in calculating the solvency liabilities
- the updated TR
- a statement of opinion from the actuary certifying that the updated TR has been determined in accordance with accepted actuarial practice

The liabilities included in the Actuarial Certification may be determined on the basis of a solvency valuation as at the determination date or a reasonable projection of the liabilities to the determination date.

For the purposes of section 19 of the Regulation, the updated TR set out in the Actuarial Certification shall be deemed to have amended the TR in the most recently filed report and shall be deemed to be the “most recently determined transfer ratio”.

### **Filing a Valuation Subsequent to Filing a Form 10**

Where a valuation report is filed subsequent to filing a Form 10, and that new valuation report has an effective date that is before the determination date of the Form 10, the TR set out in the Form 10 remains in effect and any approval or denial of approval also remains in effect.