Financial Services Commission of Ontario
Commission des services financiers de l'Ontario

Ontario

SECTION:	Actuarial Guidance Note
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TITLE:	Determination of Interest Payments Where Solvency Special Payments Are Covered by Letters of Credit -Regulation 909 s. 5
APPROVED BY:	Superintendent of Financial Services
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Note: Where this guidance note conflicts with the Financial Services Commission of Ontario Act, 1997, S.O. 1997, c. 28 (FSCO Act), Pension Benefits Act, R.S.O. 1990, c. P.8 (PBA) or Regulation 909, R.R.O. 1990 (Regulation), the FSCO Act, PBA or Regulation govern.

Note: The electronic version of this policy, including direct access to all linked references, is available on FSCO's website at www.fsco.gov.on.ca. *All pension policies can be accessed from the* **Pensions** *section of the website through the* **Pension Policies** *link.*

Purpose

Under subsection 5(3) of the Regulation, where an employer provides a letter of credit (LOC) instead of making special payments with respect to a solvency deficiency,

"*the employer is required to make interest payments with respect to the solvency deficiency, calculated at the rate of interest described in subsection (2), unless the interest payments are included in the amount of the letter of credit.*"

This Actuarial Guidance Note describes FSCO's expectations with respect to the application of this subsection and clarifies how interest payments are to be determined.

Application of Interest

A LOC must relate to the scheduled special payments that are required with respect to a solvency deficiency. Where a solvency special payment is not secured by a LOC, the employer must make the solvency special payment by the scheduled due date.

If an employer obtains one or more LOCs to secure solvency special payments, interest on those payments must be paid in cash to the pension fund unless the aggregate amount of the LOCs is sufficient to cover the required interest payments in addition to securing the solvency special payments.

Interest Rates

The interest rates used to determine the interest amount required to be paid on solvency special payments secured by a LOC should be the interest rates used to determine the solvency deficiency in the most recent report filed under section 14 of the Regulation. Where different interest rates were applied to determine the solvency deficiency, an average interest rate (weighted by relevant solvency liabilities) should be used to determine the required interest payments.

Where a schedule of solvency special payments secured by a LOC is established in a cost certificate filed pursuant to FSCO Policy A400-100 with respect to an amendment effective after the valuation date of the last filed valuation report but prior to the valuation date of the next report that is required to be filed under section 14, the interest rate to use should be the same as that used to determine the incremental solvency special payments associated with the amendment.

FSCO may request a copy of the schedules used to calculate the interest payments.

Timing of Interest Payments

Interest should accumulate on the balance of unpaid solvency special payments on a monthly basis until the expiry date of the LOC. At the end of each month the LOC is in effect, if the total of the unpaid solvency special payments and accumulated interest exceeds the amount of the LOC, the employer is expected to pay the difference on that date. Alternatively, FSCO would accept the accumulated interest to be remitted to the pension fund on a date not later than the expiry date of the LOC (prior to any renewal). For clarity, interest must continue to accrue and is compounded on a monthly basis.

Where there is a prior year credit balance (PYCB), the employer may not apply the PYCB towards the required interest payments. This is in accordance with subsection 4(3) of the Regulation which provides that the PYCB may only be applied to reduce payments attributable to normal cost and special payments.

A detailed illustration is provided in the Appendix.

Appendix – Sample Plan Holding a Letter of Credit

For the purpose of illustrating the application of interest, the following plan scenario has been assumed:

- The plan has two solvency special payment schedules with amounts payable monthly in arrears.
- Schedule 1 was determined in a most recently filed report using a discount rate of 4.00% per annum and Schedule 2 was determined in an interim cost certificate at a discount rate of 3.00% per annum.
- Schedule 1 and Schedule 2 have required monthly solvency special payments of $2,000 and $1,000 respectively.
- The employer provides a LOC in the amount of $3,000 in January, increasing by $3,000 per month until the end of June. The LOC amount remains level at $18,000 from June until its expiry date of December 31.

The table below illustrates the required interest payments that must be made by the employer upon the expiry date of the LOC.

Month	**Schedule 1** Special payments covered by LOC	Interest* accrued to Dec 31 @ **4.00%**	**Schedule 2** Special payments covered by LOC	Interest* accrued to Dec 31 @ **3.00%**	Total special payments covered by LOC	Total Interest accrued to Dec 31
Jan	2,000.00	73.21	1,000.00	27.47	3,000.00	100.68
Feb	2,000.00	66.45	1,000.00	24.94	3,000.00	91.39
Mar	2,000.00	59.70	1,000.00	22.42	3,000.00	82.12
Apr	2,000.00	52.98	1,000.00	19.90	3,000.00	72.88
May	2,000.00	46.28	1,000.00	17.39	3,000.00	63.67
Jun	2,000.00	39.61	1,000.00	14.89	3,000.00	54.50
Jul	**	0.00	**	0.00	**	0.00
Aug	**	0.00	**	0.00	**	0.00
Sep	**	0.00	**	0.00	**	0.00
Oct	**	0.00	**	0.00	**	0.00
Nov	**	0.00	**	0.00	**	0.00
Dec	**	0.00	**	0.00	**	0.00
Total	12,000.00	338.23	6,000.00	127.01	18,000.00	465.24

* The interest rates above are annual effective rates. Therefore, interest has been calculated on a compound basis.

** The employer must resume making monthly special payments that are not covered by the LOC from July onward.

Total Unpaid Solvency Special Payments with interest to Dec. 31	18,465.24
Amount of LOC	18,000.00
Interest to be paid at December 31	465.24