Finance

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Interpretation of Calculation of Solvency Deficiency in Pension Plans Containing Defined Benefit Provisions

It has come to the attention of the Office of the Alberta Superintendent of Financial Institutions (ASFI) that there is some confusion regarding the calculation of solvency deficiencies in pension plans containing defined benefit provisions.

In all likelihood, the frequency of questions has increased due to the fact that prior to recent downturns in worldwide investment markets, many defined benefit pension plans enjoyed a surplus on a solvency basis. Consequently, the calculation of solvency position of the plan had not been required, provided the actuary had opined that the solvency ratio of the plan was greater than 1.0 and that the plan did not have a solvency deficiency.

Section 2(1)(u) of the *Employment Pension Plans Regulation* (the Regulation) defines solvency deficiency as:

> "*the amount, if any, by which the plan's liabilities, determined on a plan termination basis and as of the latest review date, exceed,*
>
> *(i) in the case of a pension plan that is not terminating, the value of its assets as determined under subsection (2), and*
>
> *(ii) in the case of a pension plan that is terminating, the value of its assets as determined under subsection (2), exclusive of the items specified in subsection (2)(b)(ii)*[1]";

ASFI has generally regarded the calculation of the solvency deficiency at a particular review date to measure the "total" solvency deficiency of the pension plan. Although the calculation of the solvency deficiency is made on the hypothetical assumption that the plan had wound up as at the review date, if the Plan actually *had* wound up, the "total" solvency deficiency at the termination date immediately becomes relevant.

By including the actuarial present value of remaining solvency special payments in the solvency assets, this calculation, then, would not identify clearly the "total" solvency deficiency of a pension plan. Rather, calculating solvency deficiency in this manner would yield only the "newly established" solvency deficiency that had arisen over the inter-valuation period.

[1] Section 2(2)(b)(ii) of the Regulation means the actuarial present value of 5 years worth of special payments

Consequently, ASFI has generally questioned actuarial valuations in which solvency assets were calculated to include the actuarial present value of remaining solvency special payments (that had corresponded to previously established solvency deficiencies).

However, 2(2)(b)(ii) of the Regulation does not expressly forbid including the actuarial present value of solvency special payments in the calculation of solvency assets.

This has resulted in confusion regarding the intended application of 2(1)(u) of the Regulation as compared to the provisions of 2(2)(b)(ii).

ASFI intends to review the phrasing of 2(2)(b)(ii) to ensure that the intended application of section 2(2)(u) is to prevail. In the meantime, it is acceptable for actuaries to include the actuarial present value of solvency special payments in the calculation of solvency assets.

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