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

SECTION:	Actuarial Guidance Note
INDEX NO.:	AGN-001-Actuarial Assumptions for Filed Actuarial Valuation Reports
TITLE:	Canadian Institute of Actuaries, Practice-Specific Standards for Pension Plans effective on December 31, 2010
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.

Under the PBA and Regulation, the administrator of a pension plan that provides defined benefits is required to file, on either an annual or triennial basis, actuarial valuation reports to establish the funding requirements of the plan in accordance with the Regulation. The reports and certificates required under the PBA and Regulation must be prepared by an actuary, who must use methods and actuarial assumptions that are consistent with accepted actuarial practice.

The PBA provides authority for the Superintendent of the Financial Services Commission of Ontario (FSCO) to require the preparation of a new actuarial valuation report, where FSCO is of the opinion that the assumptions or methods used in the preparation of a report in respect of the plan are not consistent with accepted actuarial practice, or are inappropriate.

The Actuarial Standards Board of the Canadian Institute of Actuaries (CIA) introduced revisions to the CIA Standards of Practice – Practice-Specific Standards for Pension Plans, which became effective on December 31, 2010. FSCO is of the opinion that the application of some of these revisions may result in the use of assumptions which are not considered to be appropriate for an actuarial valuation report filed under the PBA and Regulation.

This Actuarial Guidance Note describes FSCO's expectations when an actuary selects assumptions that will be used in the preparation of an actuarial valuation report to be filed with FSCO for purposes of the PBA and Regulation.

In addition, the Note clarifies FSCO's expectations about the application of a new Educational Note issued by the CIA.

General

When FSCO is determining whether the actuarial assumptions used in a report filed in respect of a pension plan are appropriate, FSCO considers whether actuarial assumptions have been chosen with a level of prudence consistent with the plan's funding objectives, with due consideration to the underlying characteristics of the pension plan obligations.

FSCO closely monitors and reviews the going concern assumptions and methods selected for actuarial valuations to ensure that they are independently reasonable, are appropriate in aggregate, and incorporate margins where appropriate.

FSCO will consider, on a case by case basis, submissions from the actuary which provide support that the use of assumptions which vary from the expectations of FSCO as described in this policy, are appropriate for the pension plan.

1. <u>Margins for Adverse Deviations</u>

Section 3230.01 of the revised Standards of Practice provides that "*For a going concern valuation the actuary should ... select either best estimate assumptions or best estimate assumptions modified to incorporate margins for adverse deviations... to the extent, if any, required by law or by the terms of an appropriate engagement,...*".

In the case of a pension plan which commits the employer to provide members who retire from the plan with a fixed or ascertainable amount of pension[1], FSCO generally expects that the actuary preparing a report on the plan for filing under the PBA and Regulation will include appropriate margins for adverse deviations when choosing prudent economic and other actuarial assumptions. In selecting the actuarial assumptions and determining the appropriate margins to apply, the actuary should discuss with the plan administrator the plan's past and expected future experience and identify both the range of reasonable assumptions and their suitability, in the context of meeting the plan's funding objectives.

In the case of:

a) a multi-employer pension plan (MEPP) which is funded by fixed contributions pursuant to collective bargaining agreements, or
b) a jointly sponsored pension plan (JSPP) in which the employer or employer representatives and the members share responsibility for its funding and governance,

the actuary should discuss with the Board of Trustees or other entity responsible for the administration of the MEPP or JSPP whether it is appropriate to include margins for adverse deviations in the actuarial valuation, with due consideration to the interests of plan stakeholders and potential inequities among generations of plan members, their employers and other plan stakeholders.

[1] The employer obligations under most single employer defined benefit pension plans are of this nature.

2. <u>Discount Rate Selection and the Investment Policy</u>

In the determination of the going concern valuation discount rate, the CIA provides further guidance to actuaries in the Educational Note, *Determination of Best Estimate Discount Rates for Going Concern Funding Valuations.*

As the *best estimate* discount rate is largely driven by the investment policy of the pension plan, the actuary should, in developing the best estimate discount rate, discuss with the plan administrator whether the plan's investment policy reflects the plan's funding objectives, as well as the nature of the plan's liabilities, the demographic profile of the plan, the risk tolerances of the plan stakeholders, the investment objectives, and any other relevant factors. In the actuarial valuation report filed in respect of a plan, the actuary should provide comments on the potential risks related to meeting the plan's funding objectives, due to the investment policy adopted by the plan administrator.

3. <u>Salary Growth Assumption</u>

Previously, the Standards of Practice for pension plans explicitly required the actuary to include a salary growth assumption in the valuation of an earnings-related plan. This explicit requirement to include assumed future salary increases in a going concern valuation has been eliminated from the revised Standards of Practice for Pension Plans but is still a needed assumption under section 1700 of the General Standards of Practice.

FSCO expects that, for a final or best average earnings plan, the actuary will continue to include an assumption for future salary increases in the actuarial valuation report filed in respect of the plan.

4. <u>Active Management</u>

Section 3230.03 of the revised Standards of Practice states that the actuary may not anticipate any additional returns, *net of fees and expenses*, from an active investment management strategy except to the extent the actuary has reason to believe, based on relevant supporting data, that such additional returns will be consistently and reliably earned over the long term.

FSCO expects the guidance contained in the CIA Educational Note, *Determination of Best Estimate Discount Rates for Going Concern Funding Valuations*, to be followed in justifying any assumption for value added returns from active management contained in the actuarial valuation report filed in respect of the plan. FSCO may request, as necessary, additional information from the actuary, administrator, investment manager and/or plan sponsor for the justification of an assumption of additional returns from active management.