January 2019

Information Bulletin

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New Proposed Changes to Determination of Pension Commuted Values

The Actuarial Standards Board in Canada (ASB) has issued a new publication which proposes changes to the standards governing how pension commuted values (Commuted Values) are calculated. This follows from earlier proposals published in 2017 that were discussed in our July 2017 Information Bulletin.

The ASB has invited interested parties to submit feedback by January 31 and expects that the changes to the Commuted Value standards could be finalized in early 2019, with an effective date not before the second quarter of 2019. The ASB is also considering making changes to the mortality basis for Commuted Values and these changes could well come into effect at the same time.

The following table highlights the main changes that are proposed.

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Highlights of Proposed Changes

Topic	Current Standards	Initial Proposed Changes	New Proposed Changes
Determination of interest rate: Liquidity spread (amount to add to Government of Canada bond yields)	+0.9%	2/3 provincial spread + 1/3 corporate spread (at mid and long term)	▪ Same as Initial but spread capped at 1.5% and cannot be less than 0% ▪ Spreads to be published monthly on a publicly available website
Assumed Pension Commencement Age	Age that maximizes the Commuted Value	Age that maximizes the Commuted Value	▪ 50% at age that maximizes the Commuted Value ▪ 50% at earliest unreduced age
Rounding of Interest Rates	▪ Round to 0.10% ▪ Indexation not rounded	▪ Round to 0.10% ▪ Indexation rounded	▪ Round to 0.10% ▪ For plans with indexation, three options are provided for rounding and indexing assumption should be disclosed separately
Recomputation Period	Determined by actuary, considering applicable legislation and plan rules	Determined by plan, applicable legislation or by plan administrator. Default would be nine months.	Same as Initial
Target Pension Arrangements	No difference – Commuted Value calculated like any other plan	Share of assets approach: **Going Concern funded ratio** **Multiplied by** **Going Concern liability of the former member** GC assumptions exclude margins (i.e. best estimate)	Going Concern liability approach: **Going Concern liability of the former member** **Or** **Going Concern liability of the former member** **Multiplied by** **Adjustment related to Going Concern funded ratio per plan terms or legislation** GC assumptions include funding margins

Commentary

The proposed modifications to the interest rate assumptions (addition of a floor and ceiling on spreads and rounding for indexed plans) are relatively minor. However, it should be noted that while it was previously suggested that the change from a fixed spread of 0.90% to a variable spread would slightly lower commuted values, under the current economic environment, there is no material difference between the two approaches at this point in time. Over longer periods, we would not expect the new variable spread approach to be biased to producing either higher or lower values than the current basis.

However, the move away from an assumption that all members would commence their pension at the optimal age will reduce commuted values (perhaps materially) in plans that offer early retirement subsidies for terminated vested members. Plan administrators should be aware that the proposed approach of using two different retirement ages could involve some changes to administration systems. If the new standard is effective as early as Q2 of 2019, it will likely take much more time for administration systems to be updated. However, the standard is a minimum standard; if a plan continues to assume commencement at the optimal age while systems are being updated they would still be meeting minimum standards.

For target benefit plans, in Aon's 2017 submission to the Canadian Institute of Actuaries, we suggested that more flexibility was needed. The new exposure draft does provide flexibility as the commuted value can be either the Going Concern Liability (GCL) for the former member, or the GCL adjusted by the funded ratio, depending on plans terms and applicable legislation. We support this additional flexibility as every Target Benefit Plan is unique, and it is difficult to come up with a "one size fits all" rule that would work for all Target Benefit Plans.

Contact Information

Should you wish additional information on this topic, please contact your local Aon consultant, or send an email to info@aonhewitt.com.

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