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Ms. Leah Fichter
Executive Director Pensions Division
Financial and Consumer Affairs Authority
Government of Saskatchewan
n601 - 1919 Saskatchewan Drive, Regina, SK
S4P 4H2

RE: PENSION CONSULTATION PAPER MARCH 23, 2021

Dear Ms. Fichter:

We have prepared this document as a response to the FCAA's Consultation Paper issued March 23, 2021: A Review of the Pension Funding Framework For Single Employer Defined Benefit Plans In the Private Sector And Other Complementary Reform Measures Applicable to All Defined Benefit Plans (the "Pension Consultation Paper").

Introduction

On behalf of Aon, we thank the FCAA for undertaking this consultation process and we appreciate the opportunity to help modernize and innovate the pension regulatory environment in Saskatchewan.

The views expressed in this submission are those of Aon and we are not writing on behalf of, or to express the views of, any client of Aon.

Aon empowers organizations and individuals to secure a better future through innovative human capital solutions. We advise and design a wide range of solutions that enable our clients' success. Our teams of experts help clients navigate the risks and opportunities to optimize financial security; redefine health solutions for greater choice, affordability, and well-being; and achieve sustainable growth by driving business performance through people performance. We serve more than 20,000 clients through our 15,000 professionals located in 50 countries around the world.

Our responses to the questions posed in the Pension Consultation Paper can be found below.

We are also specifically recommending that in respect of Specified Plans and Limited Liability Plans currently exempt from solvency funding, these plans remain exempt from solvency funding and these plans be exempt from any specific Provision for Adverse Deviation requirements that may be put in place on an "enhanced" going concern basis for single employer private sector pension plans (SEPPPs).

Change the Way in Which Solvency Deficiencies Are Funded

1. ***If the solution is to modify solvency funding, which of the above options or combination of options do you feel provides the right balance between benefit security and affordability?***

   i. ***Lengthen the Amortization Period for Funding Solvency Deficiencies***

   If any form of minimum solvency funding is maintained for SEPPPs, we would recommend lengthening the amortization period in order to provide a balance between

benefit security and funding stability. A common suggestion has been to lengthen the amortization period from 5 years to 10 years.

ii. Re-Amortization of Solvency Deficiencies

We support a change to the amortization of any form of solvency deficiency or unfunded liability so that, rather than having different schedules of special payments, the solvency deficiencies or unfunded liabilities are consolidated and re-amortized at each valuation. We agree that this change would reduce contribution volatility.

iii. Solvency Reserve Accounts (SRA)

Aon encourages the implementation of a legislative framework that permits solvency reserve accounts for SEPPPs. This could help improve upon the current imbalance between the allocation of risks and rewards between plan stakeholders. The asymmetry in risks and rewards together with large and volatile solvency funding contributions has been a major contributor to the decline in defined benefit pension coverage in Canada and the introduction of a Solvency Reserve Account framework would be a positive step to correct this asymmetry.

Given the positive experience related to solvency reserve accounts in Alberta and British Columbia (and a similar concept in Quebec), we would encourage FCAA to support changes that align with the framework in these jurisdictions.

We note that in British Columbia there has been some uncertainty as to whether an SRA needs to have a separate trust account and/or separate trust document from the main pension plan or whether the SRA can more simply be a notional account within the main pension plan. A full analysis of the pros and cons of each structure is likely needed. A start on this would be that a separate trust for an SRA would be more work to establish but it would likely be clearer as to the ownership and usage of the SRA, where as a notional account would likely be far easier to set up and administer. We would recommend that the exact structure needed for an SRA be addressed in the relevant legislation.

We would also recommend that the Solvency Reserve Account framework be extended to also include any special payments toward the amortization of going concern unfunded liabilities or any additional funding towards Provisions for Adverse Deviations (PfADs) in an “enhanced” going concern funding regime.

iv. Letters of Credit (LOC)

Aon supports the use of letters of credit (LOCs) as a means to manage volatility of solvency funding requirements. We do not see a fundamental reason to limit the level of solvency funding that is secured by LOCs as LOCs would provide additional funding stability and possibly enhance benefit security. If any limits are placed on LOCs the exact threshold would be a government policy decision.

2. Are there other methods of modifying solvency funding which you feel should be considered?

We would recommend including, in the modified funding framework, a one-year lag for the commencement of the amortization period for any special payments (solvency or going concern). In other words, instead of the amortization period (and associated special payments) commencing

retroactive to the valuation date, the amortization period and special payments would commence one year after the valuation date. This would provide additional time for a plan sponsor to adjust to any increase in funding requirements that may occur as a result of an actuarial valuation.

3. ***If the period of time for funding solvency deficiencies is lengthened, what is the appropriate new time period?***

   As stated above, if any form of minimum solvency funding is maintained for SEPPPs, we would recommend lengthening the amortization period in order to provide a balance between benefit security and funding stability. A common suggestion has been to lengthen the amortization period from 5 years to 10 years.

4. ***If SRAs are allowed, under what circumstances should the employer be allowed to withdraw payments that have been made into the account?***

   It may be appropriate to set a minimum required solvency ratio threshold that needs to be maintained after any SRA withdrawal is permitted from a SEPPP. A similar threshold may also apply to the plan's going concern funded level.

   We believe that requiring a 105% minimum on both solvency and going concern funded ratios and restricting withdrawals to 20% of the available amount each year could be a reasonable policy compromise as part of a permanent solvency funding reform.

   In addition, if the plan sponsor or administrator has reason to believe the SEPPP's funded position has gone below 100% on either the solvency or going concern basis, it would be reasonable to require that any withdrawals from the SRA cease. An SRA withdrawal could also be limited to a specific time period following the valuation date of a filed funding valuation (such as 6 months, 1 year), so that up-to-date valuation information is used to determine the funded position of the plan.

5. ***If LOCs are allowed, should the amount be limited to a certain percentage of liabilities?***

   As stated above, Aon supports the use of letters of credit (LOCs) as a means to manage volatility of solvency funding requirements. We do not see a fundamental reason to limit the level of solvency funding that is secured by LOCs as LOCs would provide additional funding stability and possibly enhance benefit security.

Partial Solvency Funding or No Solvency Funding

1. ***If the current solvency funding threshold of 100% is reduced to require only partial solvency funding, is a threshold of 85% appropriate?***

   The establishment of minimum pension funding requirements is an important public policy decision that must balance benefit security with affordability. Employers are not required to provide a defined benefit (DB) pension plan. If the funding regime is skewed too heavily towards benefit security, then employers may be forced to move away from or simply not offer DB plans. If the funding regime is skewed too heavily towards affordability, then there will be an increased risk of benefit reductions if the employer is not solvent.

   Until recently, Canada may have been the only country in the world where employer provided pension plans were required to fund to the wind-up liabilities (essentially funding the cost of purchasing annuities). This type of funding regime is skewed heavily towards benefit security. Some plan sponsors have closed or modified their DB plans, as the burden of high and volatile

solvency funding contributions is too heavy. While solvency funding aims to enhance benefit security, the overall financial security of Canadians has worsened as DB pension coverage has declined.

In recent years, legislators and policy makers in several provinces have recognized the need to reform pension funding and reset the balance between benefit security and affordability. These provinces have moved to reduce or eliminate solvency funding requirements and replace them with enhanced going concern funding requirements. These approaches have provided a more reasonable balance between benefit security and affordability, and better serves the interests of all Canadians. We urge the FCAA to move in this direction.

Pension legislation has become increasingly complex and varied from jurisdiction to jurisdiction, resulting in an increasingly complicated and difficult landscape for stakeholders to navigate. Consequently, we recommend that the specific changes to the solvency funding rules be made with an eye towards simplicity and consistency across jurisdictions. We would urge the FCAA to consider aligning legislation to that of Quebec.

In regard to the question of only partial solvency funding, there would be no actuarial or economic reason for any specific funding level below 100%. The level selected would be a governmental policy decision. As you have stated in the Pension Consultation Paper *"Several jurisdictions in Canada have changed or have announced changes to their solvency funding rules. The most common method of providing relief is to reduce the solvency funding requirement from 100% to 85%."* The Consultation Paper goes on to state that *"As of the last filed actuarial valuation reports, two of the SEPPPs had a solvency ratio less than 0.85, 16 had a solvency ratio between 0.85 and 0.99, and 18 had a solvency ratio of 1.00 or greater."*

As such, establishing a minimum solvency funding threshold of 85% would appear to provide a reasonable level of balance between benefit security and funding stability as well as providing some level of harmonization with other jurisdictions. This level would also stand a good chance of already being met by the bulk of the SEPPPs registered in Saskatchewan. In addition, regulations could be added that indicate that the Superintendent can reserve the right to require solvency funding above an 85% threshold for any particular pension plan if there is specific concern, on the part of the Superintendent, about the security of pension benefits in any specific pension plan, e.g. due to higher risk of employer insolvency.

2. What is the main risk(s) that a PfAD should mitigate?

Provisions for Adverse Deviations (PfADs) perform two main roles.

First, they help to mitigate volatility in a pension plan's funded status and contribution rates that results from plan experience that is different from actuarial assumptions. The main areas of volatility are 1) economic, such as investment returns (either large fluctuations in short periods of time and/or systematic lag of investment returns over longer periods of time) that are different from asset return expectations or salary increases different than anticipated and 2) demographic, such as longevity or retirement trends, different than expected.

Second, they help to achieve the main goals and objectives for the pension plan that have been set by the plan sponsor such as benefit security and funding stability. The ability to achieve these goals relies, in part, on a plan's ability to build margin and release margin when appropriate.

As such, PfADs should mitigate the risk that actual plan experience is different than expected and support the realization of the goals and objectives of the plan through periods of such volatility.

3. What do you feel is the best method of determining the level of PfAD?

PfADs that are required by the "enhanced" going concern funding proposed should be developed in a simple, easy to understand manner. We believe that the most straight forward approach is to establish PfADs based on the various risks inherent in a pension plan's asset mix (asset/liability mismatch risk, cashflow and liquidity risk, interest rate sensitivity risk, etc.). We would make reference to both the Québec and Ontario legislation as well as the current PfAD requirements for Limited Liability Pension Plans registered in Saskatchewan.

4. Should the method of determining PfAD be different if there is no solvency funding required than if there is a certain level of solvency funding required?

We believe that the determination of PfADs (whether required by legislation or on a voluntary basis as per each plan's funding policy) is an integral part of the ongoing operation of a defined benefit pension plan and that PfADs should be established based on the risk profile of each pension plan. As such, the level of solvency funding that is required should not directly influence the overall level of PfADs established in the going concern valuation.

However, any amount of PfAD that is required by legislation should also consider any required solvency funding. As we have stated above, if the funding regime, as a whole, is skewed too heavily towards benefit security, then employers may be forced to move away from or simply not offer DB plans. Hence if some level of minimum solvency funding is required, then we would recommend that the level of required PfAD be lowered in the enhanced going concern basis so as to maintain a level of balance between benefit security and funding affordability.

Again, we are specifically recommending that in respect of Specified Plans and Limited Liability Plans currently exempt from solvency funding, these plans remain exempt from solvency funding and these plans be exempt from any specific Provision for Adverse Deviation requirements that may be put in place on an "enhanced" going concern basis for SEPPPs.

5. Should the PfAD have to be funded on current service contributions, even if the plan is in a going concern surplus?

In order to maintain an adequate level of funding of the plan's liabilities, a minimum level of PfAD should be included in the current service contributions even if there is a going concern surplus. We are also of the opinion that, in order to allow the plan's balance sheet to absorb fluctuations in plan experience, the PfAD that would be required by the "enhanced" going concern funding should only apply to the plan's current service cost and not to the plan's going concern liabilities for the purpose of determining minimum funding requirements.

Following the approach taken in British Columbia, when there is a reasonable level of surplus in a DB plan the requirement to have a PfAD on the current service cost could be removed from the minimum funding requirements. This will reduce the chances of building surpluses that are too large. For example, when assets are in excess of the greater of the going concern liabilities plus a sufficient balance sheet PfAD and the solvency funding threshold has been met, then the funding contributions would be the current service cost with no PfAD.

However, it would be reasonable that a PfAD be required to be held in the plan's liabilities for the purpose of determining if benefit improvements or withdrawals from an SRA (as referenced above) would be allowed.

6. ***If the period of time for amortizing going concern deficiencies is shortened, what is the appropriate period?***

   If minimum solvency funding is reduced below 100% for SEPPPs, it would be reasonable to shorten the amortization period for going concern unfunded liabilities in order to provide a balance between benefit security and funding stability. Similar to the Specified Plans registered in Saskatchewan the amortization period could be reduced from 15 years to 10 years.

7. ***Are there other methods of enhancing going concern funding which should be considered?***

   We would recommend including, in the modified funding framework, a one-year lag for the commencement of the amortization period for any special payments. In other words, instead of the amortization period (and associated special payments) commencing retroactive to the valuation date, the amortization period and special payments would commence one year after the valuation date. This would provide additional time for a plan sponsor to adjust to any increase in funding requirements that may occur as a result of an actuarial valuation.

8. ***Are there any other features to the funding rules which should be considered, such as consolidation of unfunded liabilities?***

   A review of the calculation of commuted values was done when the funding regime for Limited Liability Pension Plans was established. Commuted values can now be calculated under those plans using the going concern valuation basis. Certain Specified Plans (specifically the target benefit plans) registered in Saskatchewan have also recently been allowed to calculate CVs under a going concern valuation basis, however not all Specified Plans can calculate commuted values using a going concern valuation basis. This now means that different plans registered in Saskatchewan are subject to different requirements for funding and the payment of CVs. This imbalance has been recognized by the Canadian Association of Pension Supervisory Authorities (CAPSA), (i.e., 2019's Recommendations - Funding of Benefits for Plans Other than Defined Contribution Plans). A change to allow all DB plans to use a form of a going concern valuation basis to calculate and pay commuted values could provide better balance between the members remaining in all DB plans and those electing a lump sum payout.

   However, for plans where the plan members do not share in the risk of the plan (from either a benefit or contribution perspective) a member's commuted value would change based on the plan sponsors choice of asset mix (and risk appetite) – which is outside of the member's control. To bring a measure of balance to the commuted value calculation for these types of plans, the regulator could establish a standardized/benchmark asset mix that could be used to assess a reasonable discount rate that would not vary by decisions of the plan sponsor regarding asset mix. As such we would recommend that the calculation and payment of commuted values (CVs) from all defined benefit pension plans also be reviewed.

9. ***Are there any options from the previous section (Change the Way in Which Solvency Deficiencies Are Funded) which should be incorporated if only partial solvency funding is required, or if it is eliminated completely? In particular, would solvency reserve accounts and letters of credit be useful mechanisms if a solvency deficiency has to be funded only to a certain level?***

   As stated above we would support the inclusion of the following in an "enhanced going concern funding regime": Solvency Reserve Accounts, LOCs, consolidation of unfunded liabilities and

solvency deficiencies, extension of solvency amortization period to 10 years, and the inclusion of a 1 year lag for the commencement of amortization periods.

By way of explanation: not all plan sponsors will necessarily have access to all the funding relief measures noted above due to individual circumstances of each plan sponsor. Providing a number of alternatives will help to maintain benefit security and will provide more flexibility.

Full Funding on Plan Termination

1. ***Assuming the solvency funding framework is changed, are there any types of SEPPPs for which an employer should not have to fully fund a deficit if the plan is voluntarily terminated? For example, if members are required to contribute towards a solvency deficit, the framework could be structured so that only a portion of the deficit has to be funded by the employer if the plan is wound up.***

   While it is difficult to identify, on an actuarial basis, a specific type of SEPPP that should not be subject to full funding on plan wind up, we are also aware that the current SEPPPs registered in Saskatchewan were all incorporated under the current pension legislation which does not include full funding on plan wind up. If full funding on plan wind up is imposed on the existing SEPPPs, our concern is that this may create a situation where some of the plans may be terminated before such a requirement is implemented.

   We agree that the regulations could also include the ability for sharing the terminal funding between employees and the employer upon plan windup.

2. ***Are there any options presented in "Two Main Approaches" which should not require the full funding condition, if the Regulations are amended to include only that option? For example, if the only change made to the Act or Regulations is to allow a longer period of time for amortizing a solvency deficiency, should full funding on plan termination still be a condition for electing the option?***

   We would recommend that changes be implemented to the funding regime for SEPPPs without any requirement that a plan be subject to full funding on plan wind up in order to utilize the new funding regime.

Restrictions on Contribution Holidays

1. ***Should contribution holidays be restricted further than they are currently? If so, which method best protects member benefits?***

   In respect of SEPPPs, it may be appropriate to set minimum required going concern and solvency funded ratios that need to be maintained during a contribution holiday. We believe that requiring a 105% minimum on both solvency and going concern funded ratios during a contribution holiday for SEPPPs could be a reasonable policy compromise as part of a permanent solvency funding reform.

   Regarding Specified Plans registered in Saskatchewan (the public sector plans that are only subject to an enhanced going concern funding regime) we support no further restrictions being put on contribution holidays. More specifically, for Specified Plans, including a solvency funding requirement to determine eligibility for a Specified Plan to take a contribution holiday would be

contrary to the enhanced going concern funding regime. As such we would recommend that only a minimum going concern funded level be applied to Specified Plans.

In a similar fashion, Limited Liability plans registered in Saskatchewan are also only subject to going concern funding regime and so we support no further restrictions being put on contribution holidays for those pension plans.

2. ***If a plan is required to be funded at a higher level than 100% on a solvency basis and/or a going concern basis before taking a contribution holiday, what is the appropriate level?***

Please see our comments under question 1 above.

3. ***Should the ability to take a contribution holiday be determined on an annual basis, whereby a cost certificate would have to be filed each year to determine whether the plan remains in a surplus position?***

We believe that a triennial cost certificate would be sufficient with the additional requirement that if the plan sponsor or administrator has reason to believe the plan's funded position has gone below the funding threshold required to take a contribution holiday based on the type of pension plan (SEPPP, Specified Plan or Limited Liability Plan), it would be reasonable to require that any contribution holiday cease.

Annuity Discharge

1. ***If annuity discharge provisions are added to the Act, what are the appropriate conditions that a plan should have to meet in order to be eligible to qualify?***

We believe that when purchasing an annuity for a deferred or immediate pension promise at least the following conditions should apply in order to provide a full annuity discharge:

- The annuity should provide the same form and at least the same amount of pension as under the pension plan.
- To help facilitate securing annuities with provisions that are not readily available in the annuity market (such as post retirement indexation), the ability to replace the unavailable characteristics with an annuity providing similar characteristics and value should also be allowed. For example, an annuity that has indexation at a fixed rate per year could replace a pension provided by a pension plan that has post retirement indexing tied to inflation as long as it can be shown that the two forms of indexation have similar value to plan members.
- Any deficit related to the discharged portion of the benefit be immediately funded.
- Filing should occur with FCAA confirming the annuity transaction was performed in accordance with the Act and Regulations.

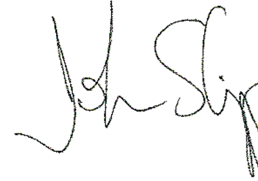
We also have the following suggestions:

- We do not believe a new valuation is necessarily required in order to secure full annuity discharge, but we do suggest that an updated cost certificate may be required.
- It is always good policy to communicate to members that an annuity purchase has occurred, however member consent should not be a requirement for full annuity discharge.

- With respect to any previous annuities purchased by a plan prior to the legislative change, a full annuity discharge should apply if it can be shown that the current requirements under the Act have been met by the annuity purchase.

Please contact us if you have any questions.

Sincerely,



David R. Larsen, FSA, FCIA
Partner
(306) 291-6476

John Slipp, FSA, FCIA
Associate Partner
(403) 290-8932