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Subject: Actuarial Bulletin No. 4 - Draft Bulletin for Industry Consultation: Reasonable Methods to Apportion Assets and Actuarial Liabilities

The Canadian Institute of Actuaries (CIA) is pleased to offer comments on the draft Actuarial Bulletin No. 4 published by the Registered Plans Directorate. The Bulletin addresses the application of subparagraph 147.2(2)(a)(vi) of the Income Tax Act (ITA), which requires that plan assets and actuarial liabilities of the defined benefit provision of a registered pension plan with more than one participating employer be apportioned among the participating employers in a reasonable manner.

Our high-level comments are with respect to the Bulletin, and not the ITA. The Bulletin provides guidelines and examples of reasonable methods to apportion assets and actuarial liabilities under this subparagraph and also addresses the funding of actuarial deficits associated with a participating employer who becomes an inactive employer.

The Bulletin does not speak to the concerns of the Canada Revenue Agency (CRA) with current practice that the proposed Bulletin is intended to remedy. As such, our comments at this time are high-level observations only and we would be pleased to engage in consultation with the CRA to understand its concerns with current practice in an effort to develop a second draft.

Pension plans designed to pool risk

Defined benefit pension plans are designed to pool risk among all plan members, and in many cases also among participating employers, in order to reduce risk for all plan members and employers. The design of many pension plans with more than one participating employer is premised on participating employers contributing the same or defined contribution rates based on the results of the plan as a whole. In most cases, participating employers have little or no control over the contribution rates set by the plan. The pooling of risk amongst a number of participating employers is part of what makes these plans work so well and pension assets and liabilities are not apportioned for these plans.

In some of these pension plans there are hundreds of different participating employers and plan members could be employed by several participating employers within a year, and employed by many participating employers during their period of accrual (e.g., industry multi-employer pension plans or pension plans that cover workers in the health care sector, such as Healthcare of Ontario Pension Plan).

The requirement to apportion defined benefit pension plan assets and actuarial liabilities between participating employers would remove the ability to pool risk amongst all participating employers and, as such, would threaten the success of the Canadian pooled-risk pension model. Another consideration is that apportioning defined benefit pension plan assets and actuarial liabilities between participating employers could be unfeasible from a practical perspective for many plans.

Proposed liability apportionment and proposed restriction on the funding of actuarial deficits

We observe that the "Liability apportionment – prorated to earnings" proposed method, with respect to an employee that is employed by different participating employers during their period of accrual, would result in a prior participating employer being allocated a liability associated with a subsequent participating employer's decisions (e.g., salary improvements). Further, this liability apportionment method is the only such method the Bulletin contemplates as being reasonable. The Bulletin could be clearer that other methods may also be reasonable, depending on the circumstances of the plan, and that these will be considered on a case-by-case basis.

The proposed restriction on the funding of actuarial deficits associated with a participating employer who becomes an inactive employer may be appropriate in certain circumstances. However, we are concerned that the proposal would be impossible to apply in the context of pension plans that pool risk amongst multiple participating employers.

Closing remarks

It is not clear what CRA's concerns are regarding current practice, and what policy objectives the Bulletin is intended to achieve.

Canada is home to many plans with multiple participating employers that pool risk, and where contribution rates are determined by the plans themselves and not controlled by any single employer. This pooled-risk model is seen as one of the greatest strengths of our retirement system. Requiring these kinds of plans to apportion assets and liabilities would result in significant administrative burden. Further, if each participating employer were required to fund based on their apportioned assets and liabilities, it could destroy this very successful model. Placing onerous or unfeasible requirements on pension plans that are designed to pool risk, which serve to counteract their strength, is counterproductive and detrimental to Canada's retirement income system. It is not clear what policy objective is achieved by imposing the requirements of the Bulletin on these kinds of plans.

We agree that it is appropriate to place limits on certain pension plans, in particular where certain apportionment methods can be manipulated and result in unfair tax deductions. However, considering the vast array of pension plan designs and structures in Canada, we do not believe it is possible to establish prescriptive rules that would cover all scenarios and it would be more appropriate to address the specific scenarios that the CRA considers abusive.

Consequently, we suggest that a set of principles be established with respect to the application of subparagraph 147.2(2)(a)(vi) and paragraph 147.2(2)(d) of the ITA. This set of principles should consider pension plan designs (e.g., pooled risk or a group of associated employers that are taxed as a single entity) where an apportionment method should not apply.

Thank you for taking the time to review our submission. If you have any questions, please contact Chris Fievoli, CIA Staff Actuary, Communications and Public Affairs, at 613-656-1927 or chris.fievoli@cia-ica.ca.

Sincerely,

[original signature on file]

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