FINAL

STANDARD OF PRACTICE FOR THE COMPUTATION OF THE COMMUTED VALUE OF PENSION BENEFITS IN CASES OF REDUCED LIFE EXPECTANCY

Effective date: April 1, 2004

PRACTICE STANDARDS COUNCIL

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MEMORANDUM

TO: All Fellows, Associates and Correspondents of the CIA practising in the area of pension plans

FROM: Luc Farmer, Chairperson of the Practice Standards Council

DATE: February 23, 2004

SUBJECT: **Standard of Practice for the Computation of the Commuted Value of Pension Benefits in Cases of Reduced Life Expectancy**

Enclosed is the final version of the Standard of Practice for the Computation of the Commuted Value of Pension Benefits in Cases of Reduced Life Expectancy. This Standard is relevant for calculations performed by an actuary to determine the commuted values to be paid in accordance with Ontario Regulation 144.

This document replaces the Exposure Draft released in November 2001. After extensive review of the comments received from the membership by the Task Force on Commutation of Pensions Due to Shortened Life Expectancy, this document includes a few minor changes.

This Standard should be read in conjunction with the *Recommendation for the Computation of Transfer Values from Registered Pension Plans* (or the *Standard of Practice for Determining Pension Commuted Values* after its effective date).

Because the process for revising this Standard commenced prior to the adoption of the Consolidated Standards of Practice, this Standard is not in CSOP format. It will be revised to conform to the format of the Consolidated Standards of Practice.

The due process for approval of this standard is the "interim due process," and this Standard has been approved by the Practice Standards Council as meeting the criteria established for adoption of a standard of practice.

The effective date of this Standard is April 1, 2004, but early implementation is encouraged.

LF

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STANDARD OF PRACTICE FOR THE COMPUTATION OF THE COMMUTED VALUE OF PENSION BENEFITS IN CASES OF REDUCED LIFE EXPECTANCY

INTRODUCTION

Recent changes to the Ontario Pension Benefits Act and regulations allow a former pension plan member, with a medical certification of less than two years life expectancy (and spousal consent), to elect a cash payment equal to the commuted value of the individual's remaining benefit entitlement. For this purpose, the commuted value is to be calculated in accordance with accepted actuarial practice. This standard establishes the accepted actuarial practice for this purpose.

1. APPLICATION

This standard of practice applies to the computation of the commuted value of pension benefits from a registered pension plan, where the right to receive the lump sum is based on Subsection 51.1 of the regulations to the Ontario Pension Benefits Act. This standard may also be applicable in other directly comparable situations.

This standard does not apply where the right to receive a lump sum is not conditional upon medical certification, under legislation or plan provisions, even if the former member is known to be terminally ill.

2. GENERAL PRINCIPLES

A. *Date of Computation and Update for Later Payment*

The lump sum value should be calculated as of the date of the medical certificate specifying that the former member has life expectancy less than two years , even if other conditions for payment of the benefit (such as spousal consent) are not met until a later date. The lump sum value should be adjusted for interest and benefits paid to the date of payment. The computation should not be adjusted to reflect the actual death or change in health of the former member after the computation date. However, if a former pension plan member becomes eligible for immediate commencement of a pension after the date of the medical certificate and prior to payment of the benefit, this eligibility should be reflected in the calculation

B. *Reflect Full Benefit Entitlement*

The lump sum value should reflect the plan member's full benefit entitlement as a deferred or immediate pensioner, as may be applicable, determined under the terms of the pension plan.

There are three possible cases:

(a) A former member with deferred pension entitlement, not eligible for immediate commencement of pension:

In this case, the lump sum value should reflect the present value of the death benefits which would be payable in respect of the former member. For this purpose, the value of the death benefit should be calculated as of the computation date, assuming the former member died as of the computation date.

(b) A former member with deferred pension entitlement, eligible for immediate commencement of pension:

In this case, the lump sum value should be the greater of the amount determined per (a) above and a value determined as if the individual had retired at the date of computation and elected the most favourable combination of the highest surviving spouse pension permitted by the plan (if there is an eligible spouse) and the longest guaranteed period available under the plan. This value should be determined as for pensioners per (c) below.

(c) A former member in receipt of pension:

In this case, the lump sum value should reflect the present value of pension payments for a period certain of four months from the date of computation, any additional guaranteed payments and any survivor benefits potentially payable.

In any of these cases, if the former member is entitled to a regular commuted value transfer based on plan provisions or legislation, not conditioned on reduced life expectancy, the amount payable should be the greater of the amount calculated in accordance with the *Recommendations for the Computation of Transfer Values from Registered Pension Plans* (or the *Standard of Practice for Determining Pension Commuted Values* after its effective date) and the amount computed, as described above.

3. ACTUARIAL ASSUMPTIONS

In all respects, other than the former member's mortality, the actuarial assumptions to be used should be the same as those specified in the *Recommendations for the Computation of Transfer Values from Registered Pension Plans* (or the *Standard of Practice for Determining Pension Commuted Values* after its effective date).

A former member's spouse entitled to survivor benefits should be assumed to have normal mortality. Thus, the lump sum payment for a pension in payment to a former member that includes a surviving spouse pension may be valued as a four month term certain annuity plus the applicable spousal pension with a four month deferred period.

4. DISCLOSURE

Disclosure should be the same as provided under the *Recommendations for the Computation of Transfer Values from Registered Pension Plans* (or the *Standard of Practice for Determining Pension Commuted Values* after its effective date). The survival period assumption should be specifically identified.