Canadian Institute of Actuaries
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Educational Note

Events Occurring After the Calculation Date of an Actuarial Opinion for a Pension Plan

Document 207007

This document was replaced by document 215004

This document was archived October 10, 2023

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Educational Note

Events Occurring After the Calculation Date of an Actuarial Opinion for a Pension Plan

Committee on Pension Plan Financial Reporting

January 2007

Document 207007

Ce document est disponible en français

Educational Notes do not constitute standards of practice. They are intended to assist actuaries in applying standards of practice in respect of specific matters. Responsibility for the manner of application of standards in specific circumstances remains that of the member in the Pension Area.

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Memorandum

To: All Members in the Pension Practice Area

From: Stephen Butterfield, Chairperson
Committee on Pension Plan Financial Reporting

Date: January 10, 2007

Subject: **Educational Note – Events Occurring After the Calculation Date of an Actuarial Opinion for a Pension Plan**

The Committee on Pension Plan Financial Reporting (PPFRC) has prepared the attached educational note to provide advice to assist pension actuaries in valuing and reporting on events that occur after the calculation date, when the actuary has determined that the event makes the entity different.

In accordance with the Institute's Policy on Due Process for Approval of Practice-Related Material other than Standards of Practice, this educational note has been approved by the Committee on Pension Plan Financial Reporting (PPFRC), and received final approval for distribution by the Practice Council on December 6, 2006.

As outlined in subsection 1220 of the Standards of Practice, "the actuary should be familiar with the relevant educational notes and other designated educational material," and be aware that a "practice which the notes describe for a situation is not necessarily the only accepted practice for that situation and is not necessarily accepted actuarial practice for a different situation," and that "educational notes are intended to illustrate the application (but not necessarily the only application) of the standards, so there should be no conflict between them."

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INTRODUCTION

The purpose of this educational note is to assist pension actuaries in valuing and reporting on events that occur after the calculation date, when the actuary has determined that the event makes the entity different.

This educational note does not provide assistance on how to determine whether an event makes an entity different and, therefore, whether the actuary would reflect the event in his or her calculations or report. Rather, the purpose of this educational note is to provide pension actuaries with guidance on how to quantify and report on an event when the actuary has already determined that the event does make the entity different. The actuary would refer to subsection 1520 of the Standards of Practice for details on how to determine whether an event makes an entity different.

While the most common such event is a plan amendment that improves the benefits under a pension plan, this educational note is also intended to apply to other events such as a reduction in benefits, a significant decrease in the plan membership, etc.

This educational note was prepared in contemplation of a regular funding valuation, including the going concern valuation, hypothetical wind-up valuation and solvency valuation. Certain aspects of this educational note may not be applicable in certain special circumstances, such as actual wind-up valuations, accounting valuations or valuations for other purposes.

Finally, some legislators have regulations or have issued policies describing the expected methods of reporting on plan amendments (for example, see policy A400 - 100 Actuarial Filing for Plan Amendments from the Financial Services Commission of Ontario). The actuary should take into consideration any such policies and regulations as well as the information contained in this educational note.

DEFINITIONS

This educational note makes use of terms defined in subsection 1110 of the Standards of Practice. For convenience, these terms are reproduced here:

“Calculation date” is the effective date of a calculation; e.g., the balance sheet date in the case of a valuation for financial statements. It usually differs from the report date.

“Internal user” is the actuary’s client or employer.

“External user” is a user who is not an internal user. Internal user and external user are mutually exclusive.

“Report date” is the date on which the actuary completes the report on his or her work. It usually differs from the calculation date.

“Subsequent event” is an event which occurs after a calculation date but before the corresponding report date.

This educational note separately considers:

1. events that are definitive or virtually definitive <u>before</u> the report date (a subsequent event); and
2. events that are definitive or virtually definitive <u>after</u> the report date.

The reporting of the financial implications of events that become definitive or virtually definitive after the calculation date has commonly been referred to as an "**interim actuarial opinion.**" It is noted that this term does not exist in the Standards of Practice. When an actuary provides an opinion about the financial position of a plan as at a certain calculation date, he or she would comply with all aspects of the Standards of Practice. This includes, among other things, that the data are sufficient and reliable, the assumptions are, in aggregate, appropriate and the methods are appropriate, at that calculation date. Therefore, an opinion that is based on assets determined at a certain calculation date but liabilities calculated using assumptions that are not appropriate as at this calculation date would not be in accordance with the Standards of Practice.

EVENTS THAT ARE DEFINITIVE OR VIRTUALLY DEFINITIVE BEFORE THE REPORT DATE (I.E., A SUBSEQUENT EVENT)

Under subsection 1520 of the Standards of Practice, if an event is definitive, or virtually definitive, before the report date, it is a subsequent event and it should either:

- be taken into account in the calculations, or
- be disclosed in the report but not taken into account in the calculations.

If the actuary chooses to disclose the event but not take it into account in the calculations, paragraph 1820.22 of the Standards of Practice requires the actuary to report that the event will be taken into account in a future report.

If the event is to be taken into account in the actuary's calculations, it could be done in one of the following three ways:

a) One Actuarial Opinion

The actuary could provide an opinion on the financial position of the plan (both on a going concern and hypothetical wind-up bases) as at the calculation date by valuing all benefits, including those benefits arising out of the event, using appropriate data, methods and assumptions as at the calculation date. Subject to regulatory and legislative considerations, the increased normal cost and special going concern and solvency payments associated with the event could either:

- commence at the calculation date, even if the effective date of the event falls at a later date, or
- commence at the effective date of the event.

Note, however, that under the second option, the assumptions used to determine the increased normal cost and special going concern and solvency payments would be appropriate as at the calculation date, not the effective date of the event.

b) Two Separate Actuarial Opinions – Reflecting the Financial Positions at Two Dates

In lieu of one opinion at one calculation date, the actuary could prepare a report that provides distinct financial positions at two separate calculation dates. The data, methods and assumptions used to determine the financial positions would be appropriate at each respective calculation date (i.e., the valuation of assets and liabilities for each financial position would be consistent and would be appropriate at the respective calculation dates). The first opinion would not include provision for the subsequent event. The second opinion would include provision for the subsequent event.

c) ***Two Separate Actuarial Opinions – One Reflecting the Financial Position at the First Calculation Date and One Reflecting the Financial Impact of the Subsequent Event***

Under this approach, the actuary would prepare an opinion on the financial position of the plan at the calculation date, excluding provision for the subsequent event. A second opinion would then be prepared at the effective date of the subsequent event that reflects the financial impact of the subsequent event, but which does not opine on the financial position of the plan as a whole. For example, the second opinion may state that the subsequent event increases the going concern actuarial liability by $x, and the hypothetical windup liability by $y and provide information on the contributions required to fund these additional liabilities. However, the second opinion would not state the financial position of the plan at the effective date of the subsequent event, since the original benefits and the assets are not being revalued. Under this approach, the data, methods and assumptions used to determine the financial impact of the subsequent event would be appropriate as at the effective date of the subsequent event (i.e., the second calculation date) and may be different from the data, methods and assumptions applicable at the first calculation date.

As this method does not re-measure the financial position of the plan at the effective date of the subsequent event, it may not be appropriate for determining the funding requirements of the subsequent event when the plan is in a surplus position as of the original calculation date. In particular, it would not be appropriate to opine that the surplus as at the original calculation date is sufficient to meet the additional funding requirements that arise at the second calculation date.

Selection of Appropriate Method

The choice of which method to use to reflect the financial implications of the event will depend on various factors including:

- the type of event;
- the relative significance of the financial impact of the event;
- the funded status of the plan on both a hypothetical wind-up basis and a going concern basis;
- legislative requirements;
- the plan sponsor’s funding policy; and
- the length of time between the calculation date and the effective date of the event.

Some observations include the following:

- Method a) would typically be preferred if the date of the event was shortly after the calculation date, particularly if the event is known prior to the report date.
- Method b) would typically be preferred if there was a long period of time between the original calculation date and the date of the event. This method may further be preferred if there have been material changes to the membership data since the original calculation date, or if it is necessary to opine about the financial position of the entire plan at the event date.

- Method c) would not normally be appropriate if the actuary would opine on the funded status of the entire plan following the event. For example, consider a plan that was in a surplus position at the original calculation date and an amendment improves benefits at a subsequent date. The use of method c) would not normally enable the actuary to opine on whether the actuarial surplus at the original calculation date was sufficient to fund the plan improvements. A related situation may arise when legislation or regulations prohibit plan improvements unless a plan meets certain funding thresholds. Generally, the actuary would not be able to opine on whether the entire plan met such funding thresholds unless the actuary valued the entire plan, and not only the plan improvements.

EVENTS THAT ARE DEFINITIVE OR VIRTUALLY DEFINITIVE AFTER THE REPORT DATE

After a report date, the actuary does not have to seek additional information as to whether an event affecting the financial position of the plan has occurred. However, if an actuary becomes aware of an event that becomes definitive or virtually definitive after the report date, then the actuary may need to withdraw or amend the report. The actuary would be guided by paragraph 1820.33 of the Standards of Practice to determine whether a post report event requires the withdrawal or amendment of a report. Briefly, paragraph 1820.33 states that if the additional information were classified as a subsequent event had it been revealed prior to the report date, and it would have been taken into account in the calculations, then it invalidates the report.

If the event does not require the withdrawal or amendment of the report, then the actuary is under no obligation to report on the financial implications of the event. However, the actuary may be directed by an internal user or an external user to prepare a report which does reflect the financial implications of the event. In this situation, the actuary may apply the methods described in b) or c) above.

Under b), the actuary's report would include information on the entire financial position of the plan, at a revised calculation date. Accordingly, under this option, the actuary is really preparing a complete new opinion and new report at a revised calculation date. The new report would be subject to the normal requirements with respect to opining upon the suitability of the data, methods and assumptions as at the revised calculation date.

Under c), the actuary's report would only include information on the financial implications of the event itself. These financial implications would be determined at a revised calculation date and the actuary would be required to opine upon the suitability of the data, methods and assumptions at the revised calculation date.

FINAL COMMENT

The above guidance requires that the data, methods and assumptions be appropriate based on the calculation date. Note that this does not mean that membership data would be collected as of each calculation date. Rather, it would be permissible to project membership data from a previous date to a calculation date, provided that the actuary is comfortable that the resulting data are sufficient and reliable for the purposes of the valuation.