

Newsletter

Supplemental Pension Plans

Newsletter 27

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Converting defined benefit provisions into defined contribution provisions

To amend a pension plan in order to convert the defined benefit provisions into defined contribution provisions, the plan administrator must obtain the Régie des rentes du Québec's authorization. Accordingly, the administrator must meet certain requirements set by the Régie and the *Supplemental Pension Plans Act*.

This *Newsletter* informs plan administrators and other concerned parties of these requirements.¹ It replaces *Newsletter* number 3, *Converting a defined benefit pension plan into a defined contribution plan*, which was written before the *Act* came into effect.

What is a conversion?

With a conversion, the benefits already accumulated in a pension plan are converted to change their form.

If the plan provides that only the benefits accumulated after the effective date of the amendment will be under the defined contribution provisions, and the benefits accumulated before that date remain under the defined benefit provisions, a conversion is not considered to have taken place within the

meaning of the *Act*. This amendment therefore does not require the Régie's authorization.

Similarly, if the plan converts the defined contribution provisions — but continues to calculate those benefits under the defined benefit provisions and provides that the members are entitled to the greater of the amounts between the account balance and the benefit they would have received had there been no amendment — no real conversion is considered to have taken place. This amendment also does not require the Régie's authorization.

It is not necessary for all the benefits to be converted for an authorization to be required. For example, an authorization will be required if the conversion affects only the benefits of one category of members covered by the plan.

Normally, a plan is amended to provide that the benefits accumulated after the amendment's effective date will be under the defined contribution provisions and that, **for the members who have given their consent**, the benefits accumulated before that date will fall under the defined contribution provisions. In such a case, only the latter amendment is considered a conversion.

1. The requirements concern members subject to the *Supplemental Pension Plans Act*. For members subject to another law, that law prevails.

Newsletter

Supplemental Pension Plans

Consent of members

Section 22 of the *Act* provides that the conversion can apply only to those members who have given their consent.

In addition, since a conversion may later reduce the value of members' benefits, section 20 of the *Act* provides that, unless all affected members have consented and the Régie has given its authorization, the conversion cannot take effect before the date on which the notice informing members of the proposed amendment is sent or, if the conversion has been determined by collective agreement, before the effective date of that agreement. The same applies to an amendment to convert the benefits accumulated after the effective date of the amendment into defined contribution benefits.

Each affected member must give their **individual and explicit** consent. Consent is required even if the amendments were negotiated as part of a collective agreement. In addition, a member who has not expressed his or her views cannot be considered to have given consent.

Even if the affected members give their consent, the conversion cannot affect pensions in payment or pensions whose payment has been suspended because of a return to work.

The plan administrator must inform the Régie in writing whether all affected members have consented to the conversion. If the conversion is to take effect before the date on which the notice is sent or the effective date of the collective agreement, the administrator must also indicate whether all the affected members have agreed to the conversion's effective date.

If some members have not agreed to the conversion, the plan must continue to provide for the benefits payable to them.

Information for members

Notice of change

The plan administrator must send active and non-active members the notice required before any amendment can be registered. This notice must be sent to each member. Posting the notice in the workplace or publishing it in a daily newspaper is not sufficient. Where the conversion has been determined by collective agreement, it is not required to send a notice to members covered by the agreement. However, a notice must be sent to members not covered by the agreement (e.g., retirees).

A copy of this notice must be sent to the Régie with the application for registration of the amendment.

Document for the purpose of consent

In order for the affected members to make an informed decision, the Régie requires that they be sent a document, before they give their consent, that clearly describes the conversion's effect on their benefits. The document must contain the following information as at the conversion date:

- 1) the annual amount of the normal pension that would be payable for the years of service credited to the member under the provisions that applied before the conversion;
- 2) the annual amount of any other benefit that could be payable to the member if he or she becomes disabled, dies or ceases to be employed or an active member, under the provisions that applied before the conversion and the rules that will apply after the conversion;
- 3) if the plan provides for early retirement conditions that are more generous than an actuarially equivalent pension or a bridging benefit, and the member does not meet the eligibility requirements, the benefits for which he or she is not eligible must be indicated;
- 4) member contributions, with interest;

Newsletter

Supplemental Pension Plans

- 5) the value of the benefits that will be credited to the member's account if he or she agrees to the conversion;
- 6) the additional sum, if applicable, that will be credited to the member's account if he or she agrees to the conversion;
- 7) in the case of a plan whose benefits vary according to progression of salary, the assumptions used in the actuarial valuation to take into account salary increases;
- 8) if applicable, the unfunded portion of the benefits and the steps taken by the employer to credit the full value of the benefits to the member's account;
- 9) information regarding the interest on the value of the benefits between the valuation date and the date they are paid into the member's account, including the interest on the unfunded portion;
- 10) a mention that the actuarial valuation report can be obtained from the plan administrator for consultation, with the exception of personal or financial information concerning other members.

A copy of this document must also be sent to the Régie with the application for registration of the amendment.

Minimum amount

The amount credited to each member's account must be at least equal to the value of his or her benefits if the plan was terminated on the conversion date. That amount must include the value of excess member contributions and additional pension benefits, as well as any benefits ancillary to any pension to which the member would have been entitled if he or she had retired on the day preceding the date of conversion.

However, since there is no termination, section 62 of the *Act* must also be taken into account. Where the defined benefit provisions vary according to salary increases, the value of benefits must be

established by projecting the pension that members would have received if the plan had continued to take salary increases into account up to the presumed date they ceased active membership or the end of the period of continuous employment, depending on the plan text. In other words, the date on which members would theoretically cease active membership or their period of continuous employment must be determined as well as the salary they would theoretically earn on that date.

The same assumptions that were used to determine plan liabilities on a funding basis must be used to determine the presumed date of end of active membership or period of continuous employment as well as the salary increases. Regarding the latter element, in conformity with the *Standards of Practice* of the Canadian Institute of Actuaries, the rate of increase should be equal to the inflation rate used for calculating the value of the benefits on the date of cessation of active membership, increased by 1%, unless it can be shown that past salary increases for the group affected by the conversion were lower. If the sum calculated is greater than the maximum allowed by the Canada Revenue Agency, the plan administrator must pay the member the surplus, pursuant to section 63.1 of the *Act*.

Surplus assets

It is not required to allocate surplus assets on the conversion date. The surplus remains in the plan for all members, unless the amendment to convert benefits specifies that they be allocated to members.

Deficiency of assets

If plan assets are insufficient to meet all its commitments, the plan continues to be subject to the funding rules under the *Act*. The amortization payments made are then divided among members' accounts in proportion to their respective value, taking into account the benefits that remained under the defined benefit provisions, as applicable.

If the benefits of a member who has agreed to the conversion must be paid before the amortization payments have been fully credited to his or

Newsletter

Supplemental Pension Plans

her account, adjustments must be made under sections 145 and 146 of the *Act*. In such a case, the deficiency of assets is considered to be the “value of the benefits [...] which cannot be paid.” Therefore, only the sums credited to the member’s account can be paid initially, unless the exception provided for in section 145 can be applied, in which case the balance must be funded and paid within the time limit set in section 146.

Interest

If the converted plan is fully solvent, the benefits bear interest at the pension fund’s rate of return between the valuation date and the date they are credited to the member’s account.

If the plan is not fully solvent:

- a) the portion corresponding to the degree of solvency bears interest at the pension fund’s rate of return between the valuation date and the date it is credited to the member’s account; and
- b) the unfunded portion bears interest at the rate specified in the actuarial assumptions between the valuation date and the date it is paid into the fund, then at the pension fund’s rate of return between the date it is paid into the fund and the date it is credited to the member’s account.

Actuarial valuation

The actuarial valuation must be accompanied by a list of the members affected by the conversion as well as their personal information: full name, date of birth, sex, salary used, recognized years of service, benefits accumulated, value of benefits, member contributions accumulated and share of the surplus assets, if applicable.

Where the plan has retirees or other members with benefits under the defined benefit provisions, the actuarial valuation must include the information normally required for such provisions. For those members, a periodical actuarial valuation continues to be required, unless their benefits are guaranteed by an insurer and the plan therefore has only defined contribution provisions and guaranteed benefits. The persons whose benefits have been guaranteed in this way remain plan members and keep all their rights, specifically the right to transfer when they cease active membership.

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